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**The Invisible Recession of 2016**

By NEIL IRWIN
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Sometimes the most important economic events announce themselves with huge front-page headlines, **stock market** collapses and frantic intervention by government officials.

Other times, a hard-to-explain confluence of forces has enormous economic implications, yet comes and goes without most people even being aware of it.

In 2015 and 2016, the United States experienced the second type of event.

There was a sharp slowdown in business investment, caused by an interrelated weakening in emerging markets, a drop in the price of oil and other commodities, and a run-up in the value of the dollar.

The pain was confined mostly to the energy and agricultural sectors and to the portions of the manufacturing economy that supply them with equipment. Overall economic growth slowed but remained in positive territory. The national unemployment rate kept falling. Anyone who didn't work in energy, agriculture or manufacturing could be forgiven for not noticing it at all.

Yet understanding this slump -- think of it as a mini-recession -- is important in many ways.

It helps explain the economic growth spurt of the last two years. The end of the mini-recession in the spring of 2016 created a capital spending rebound that began in mid-2016, and it has contributed to speedier growth since. **Oil prices** have reached four-year highs, a major factor in a surge in business investment this year.

It helps explain some of the economic discontent evident in manufacturing-heavy areas during the 2016 elections. It offers warnings for where the next downturn might come from, and shows how important it is for policymakers to remain watchful and flexible about unpredictable shifts in the global economy.

Most important, the mini-recession of 2015-16 offers a cautionary tale for any policymaker who might want to think of the United States as an economic island.

The episode is stark evidence of the risk the Trump administration faces in threatening economic damage to negotiate leverage with other nations on trade and security. What happens overseas can return to American shores faster and more powerfully than once seemed possible.

How it happened

The mini-recession defies neatness. It's a story of spillovers and feedback loops and unintended consequences. But here's a summary:

In 2015, Chinese leaders were concerned that their economy was experiencing a credit bubble, and they began imposing policies to restrain growth. These worked too well and caused a steep slowdown. That in turn caused troubles in other emerging nations for whom China was a major customer.

Meanwhile, the Federal Reserve, finally growing confident that the United States economy was returning to health, made plans to end its era of ultra-easy monetary policy.

As the Fed moved toward tighter money, its counterparts at the European Central Bank and the Bank of Japan were going in the opposite direction. The prospect of higher interest rates in the United States and lower rates in the eurozone and Japan fueled a steep rise in the value of the dollar on global currency markets.

That in turn made China's problems worse. China had long pegged the value of its currency to the dollar, so a stronger dollar was also making Chinese companies less competitive globally. When China attempted to reduce this burden by loosening the peg in August 2015, it faced capital outflows, making the economic situation worse.

Moreover, across major emerging markets, many companies and banks had borrowed money in dollars, so a stronger dollar made their debt burdens more onerous.

Put it all together, and when the Fed moved toward raising interest rates -- as it eventually did in December 2015 -- it was essentially making financial conditions tighter and therefore slowing growth across big swaths of the world.

The slowdown across emerging markets, in turn, meant less demand for oil and many other commodities. That helped cause their prices to fall. The price of a barrel of West Texas Intermediate crude oil fell to under $30 in February 2016 from around $106 in June 2014. The drops in the prices of metals like copper and aluminum, and agricultural products like corn and soybeans, were also steep.

That only heightened the economic pain for the many emerging economies that are major commodity producers, such as Brazil, Mexico and Indonesia.

Given falling prices and high debt loads among energy producers in the United States, the markets for stocks and riskier corporate bonds came under stress, especially in early 2016. That generated losses for investors and fears about the overall stability of the financial system.

Each of these forces has connections to the others. It wasn't one problem, but an intersection of a bunch of them. That made it devilishly hard to diagnose, let alone to fix, even for the people whose job was to do just that.

The view from Washington

When Federal Reserve officials meet eight times a year to set interest rate policy, their job, assigned by Congress, is to figure out what is best for the United States economy. Their job isn't to set a policy that will be best for China or Brazil or Indonesia.

Entering 2015, things were looking pretty good for the United States.

Inflation was below the 2 percent level the Fed aims for, but the traditional economic models on which the central bankers had long relied predicted that it would start to rise thanks to a rapidly falling unemployment rate.

Even when prices for oil and other commodities started falling in the middle of the year, the Fed's models viewed it as a positive for the overall economy. Sure, some oil drillers and farmers might experience lower incomes, but consumers everywhere would enjoy cheaper gasoline and grocery bills.

Although officials spent a lot of time monitoring the global economy, the fact remained that the United States wasn't as dependent on exports as many smaller countries. The 2008 financial crisis had shown how the American and European banking systems were deeply intertwined, but the same couldn't be said of the ties with Chinese banks.

In other words, through the summer of 2015 it sure looked to many Fed officials as if the sound move was to start raising interest rates.

At the Treasury Department, which is responsible for the United States' currency policies, it seemed well into 2015 that the strengthening dollar was mostly benign.

''There was a sense that the U.S. was doing well and the rest of the world was not doing very well,'' said Nathan Sheets, a Treasury under secretary at the time and now chief economist at PGIM Fixed Income. ''It was driven by strong U.S. fundamentals.''

 

But in late summer 2015, **financial markets** started to react more violently to the feedback loop of global currencies and commodities. It started to seem as if some of the old rules of thumb -- about how a rising dollar or falling **oil prices** might affect the economy -- might not apply.

Perhaps the economics models used by forecasters had become outdated, failing to fully account for the ways surging energy production had become more intertwined with the manufacturing sector and the **financial markets**.

"These things were all interconnected in different ways, and they all cycled back on the same industries and parts of the economy," said Jay Shambaugh, a member of the Obama White House Council of Economic Advisers at the time. Still, distilling that complex story into crisp memos for senior officials was no easy task.

"You have to make memos short and to the point in the White House, and it was hard to say what exactly we thought was happening," he said.

Behind closed doors at the Fed, officials started debating whether this outburst of **volatility** in markets really posed a risk to the overall economy. Should they stick to their plans to raise interest rates steadily, or slow down?

Over two days in October, the debate played out publicly.

Stan Fischer, the vice chairman of the Fed, was reluctant to adjust the planned rate increases, not wishing to let swings in **financial markets** dictate policy.

"We do not currently anticipate that the effects of these recent developments on the U.S. economy will prove to be large enough to have a significant effect on the path for policy," he said in a speech in Lima, Peru, on Oct. 11, 2015.

Lael Brainard, a Federal Reserve governor who had worked on international issues at the Treasury, was quite a bit more worried.

"There is a risk that the intensification of international cross currents could weigh more heavily on U.S. demand directly, or that the anticipation of a sharper divergence in U.S. policy could impose restraint through additional tightening of financial conditions," she said on Oct. 12 in Washington.

Ms. Brainard was right.

How the damage played out

The vicious circle of a stronger dollar, weaker emerging market growth and lower commodity prices caused spending on certain types of capital goods to plummet starting in mid-2015.

Spending on agricultural machinery in 2016 fell 38 percent from 2014 levels; for petroleum and natural gas structures -- think oil drilling rigs -- the number was down a whopping 60 percent.

The oil and gas exploration boom tied to fracking technology came to a halt with energy prices at rock-bottom levels, and with it sales of equipment tied to that boom.

With the fall in domestic capital investment in those industries and with weakness overseas, companies in related industries took it on the chin. Caterpillar, the maker of heavy equipment, had 30 percent lower revenue in 2016 than 2014.

In large segments of the economy, by contrast, it was business as usual. Business spending on investments like computers and office buildings kept rising, as did consumer spending.

Still, the industrial sector downturn was powerful enough to turn a strong expansion into a weak one. Overall growth fell to 1.3 percent in the four quarters ended in mid-2016, from 3.4 percent in the preceding year.

The national economy kept adding jobs. But Harris County, Tex., which encompasses energy-centric Houston and its near suburbs, shed 0.8 percent of its jobs in that span. In Peoria, Ill., hometown of Caterpillar, employment fell 3.2 percent.

In effect, this was a localized recession -- severe in certain places, but concentrated enough that it did not throw the overall United States economy into contraction.

In Williston, N.D., where the economy had been booming for years because of a surge in oil and natural gas drilling on the Bakken oil patch, businesses of all types closed or slashed wages.

"It varies week to week, but every week keeps getting worse," Marcus Jundt, owner of a restaurant, the Williston Brewing Company, told CNBC in March 2016. "We don't know where the bottom is, but we're not there yet."

But it could have been worse.

How it ended

When Janet Yellen assumed leadership of the Federal Reserve in early 2014, she inherited an economy that had been expanding steadily for years, with a great deal of help from the Fed's interest rate policies.

Deciding how and when to pull that support -- when to raise interest rates, which had been near zero for more than six years -- was set to be the defining choice of her tenure.

In 2015, with signs that the United States economy was returning to health, she and her colleagues believed it was time to begin raising interest rates. She is a leading labor market scholar who spent a career studying, among other things, how a tight labor market can eventually feed through to inflation.

In July of that year, with stirrings of the emerging markets disruption, the unemployment rate was 5.2 percent, not much above the level Fed officials believed was consistent with a fully healthy labor market. Then the turmoil of August began.

Ms. Yellen elected not to raise rates in September, waiting for more evidence that the economy was truly on track and that the emerging market troubles wouldn't do too much damage to the domestic economy. But by December she judged that the situation had stabilized enough to raise rates.

At the same time, the Fed revealed forecasts indicating that its senior officials expected to raise interest rates four more times in 2016. Within weeks, global markets were sending a message: Not so fast.

The dollar kept strengthening, the price of commodities kept falling, and the Standard & Poor's 500 dropped about 9 percent over three weeks in late January and early February. Bond yields plummeted, suggesting that the United States was at risk of recession.

In mid-February 2016, the financial leaders of the world's most powerful nations were set to convene in a Shanghai for the periodic G20 summit. With global markets in turmoil, the great question was: Can the officials rein in these forces?

The official statement released by the participants in the summit contained multiple nods to the turbulence, acknowledging risks from "**volatile** capital flows" and falling commodity prices. But more important than any words was what followed in the following weeks.

Two days after the summit, China lowered its reserve requirement on banks, essentially opening the spigot for more lending. In the months that followed, it would put in tighter controls on the movement of capital outside the country, and seek to tie the value of the yuan less closely to the dollar.

Three weeks after the summit, the Fed had another policy meeting. Rather than raise interest rates further as had been envisioned in December, Fed officials declined to raise rates -- and steeply reduced their expectations of how much further they would raise rates over the remainder of 2016.

Together, these steps were enough to end the vicious cycle. The dollar stopped appreciating and started dropping. **Oil prices** bottomed out and began a recovery. In the United States, capital spending was growing again by the summer of 2016.

What really happened in Shanghai?

Some analysts of **financial markets** have put a conspiratorial bent on the concerted action from the two sides of the Pacific, speculating that leaders had made a secret deal at the G20 meeting in February 2016. They call it the "Shanghai Accord"-- essentially, that the Fed would hold off on rate increases if the Chinese also took actions of their own.

Ms. Yellen said it's not so. She said in an interview that there was an extensive exchange of views and information with the Chinese delegation in Shanghai, but that there were no promises or explicit agreements.

 

"I realize it looked to much of the world like some kind of secret handshake deal," she said. "This wasn't a deal. This was the global economy and capital markets affecting the U.S. outlook, and the Fed being sensitive to that, taking that into account and its influencing policy appropriately."

The Fed, she said, did what it thought was best for the United States economy without knowing exactly what the Chinese would do.

Mr. Sheets, the former Treasury official, also dismissed the idea of some secret agreement.

"It's just not how it works," he said. "There were a lot of meetings. A lot of bilaterals and quadrilaterals. You meet with your counterparts and talk about the global economy and think about the challenges and what might be done. But there was nothing agreed behind closed doors that was not part of the formal statement."

Even if there was no formal secret agreement, the result -- leaders of the world's two biggest economies squarely focused on the risks that the situation presented -- turned out to be enough.

The lessons

The impact of the global commodity-currency spiral of 2015-16 is evident from a glance at the economic statistics. It is less so in the economic debates of 2018.

First, while the Trump administration has claimed full credit for a surge in business investment, the bounce-back from the mini-recession is a major factor.

White House economists have presented charts showing a surge starting in the fourth quarter of 2016, when the election took place. But that turnaround began in mid-2016 by most measures, not late 2016 as suggested by the White House's "six quarter compound annual growth rate" measure.

Second, the mini-recession might well have affected some political attitudes during the 2016 election. While the economy was in pretty good shape for people in large cities on the coasts, 2016 was rough for a lot of people in local economies heavily reliant on drilling, mining, farming or making the machines that support those industries.

A poll in October 2016 by an agriculture trade publication, Agri-Pulse, found that 86 percent of farmers were dissatisfied with the way things were going in the United States.

Third, economic policymakers need to display the flexibility to respond to incoming information, even when it doesn't fit their own forecasts or preconceptions.

If Ms. Yellen had been more stubborn about sticking to the plan to keep raising rates through 2016 because of her training as a labor market economist, the result might well have been an actual recession. "She's always learning," said Julia Coronado, president of MacroPolicy Perspectives, "and not so egotistical that she's wedded to one view of the world."

Finally, it shows the global economy is so interconnected that events in Shanghai or São Paulo can cause unpredictable effects in faraway places.

In the last year, the Trump administration has been lobbing tariffs at China and other major economic partners to extract more advantageous terms for trade. But the mini-recession warns of the risk of ricochet.

Like it or not, the complexity of our global connections means that policy can't just focus on the home front. In 2016, we learned that lesson the hard way, even if not everybody was paying attention.

DRAWING (DRAWING BY JIALUN DENG); CHART: The Mini-Recession of 2015-16 (Source: Bureau of Economic Analysis) (BU7)

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THE WALL STREET JOURNAL.

Markets

**Copper Extends Losing Streak in Third Quarter; Investors, analysts waiting for November meetings between leaders of the world's two largest economies in hopes of a compromise on trade**

By Amrith Ramkumar
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Corrections & Amplifications Bart Melek is head of commodity strategy at TD Securities. An earlier version of this article incorrectly said he was head of commodity strategy at TD Ameritrade. (Oct. 1, 2018)

Global investors bruised by copper's 15% tumble this year are looking ahead to a November deadline for the U.S. and China to resolve a tariff fight.

Copper has fallen in three straight quarters, the longest such stretch since 2015. Steady production of the metal along with signs of slowing demand from China have weighed on sentiment this year, analysts say. Front-month futures fell 5.6% in the third quarter.

China is the world's largest commodity consumer, accounting for roughly half the world's copper demand. Investors have become sensitive to signs of weakness in the nation's economy in recent months as a trade spat between the U.S. and China drags on.

Tensions between the world's two largest economies battered prices of resources across the board this summer, but the move in copper is notable because of its heavy use in construction and manufacturing. That means a weaker global growth outlook caused by an escalating trade dispute would likely dent demand.

Now, analysts are waiting for planned November meetings between President Trump and Chinese leader Xi Jinping to see if the two countries will be able to reach a compromise on trade. Copper prices have risen 9% from their mid-August low on these hopes, as well as on signs that the Chinese government wants to keep growth steady in its nation.

"The market is behaving as though we are going to get some kind of deal," said Bart Melek, head of commodity strategy at TD Securities. "But it can't be assumed easily that a deal is going to get done."

Analysts say data showing stable supply around the world and weakness in the Chinese economy could keep money managers cautious on industrial metals. Data earlier in September showed investment in factories, railways and other projects in China grew in the first eight months of the year at its slowest pace in more than a quarter-century.

Hedge funds and other speculative investors have pared back **bearish** bets on copper prices lately—another sign that sentiment toward the metal could be improving.

**Bullish** bets by speculators exceeded **bearish** wagers for the first time since early July during the week ended Sept. 25, Commodity Futures Trading Commission data show.

Investors are also monitoring swings in the dollar. For much of the year, a stronger dollar has made copper and other commodities denominated in the U.S. currency more expensive for overseas buyers. The dollar climbed to a 15-month high in August but has since come down 0.8%, relieving some pressure on commodities.

"We still see upside in the metals, but certainly I don't think the trajectory is as high as it once was," Mr. Melek said.

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THE WALL STREET JOURNAL.

Heard on the Street
Markets

**Tesla Gets a Second Chance; SEC settlement will give Tesla shares a boost, but new chairman has a difficult task ahead**

By Charley Grant
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30 September 2018
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Who wants to supervise Elon Musk?

The Securities and Exchange Commission has settled the fraud charges against Tesla Inc.'s embattled leader. The settlement calls for, among other things, the installation of a new chairman to oversee Mr. Musk. The settlement will allow him to remain as chief executive.

That is clearly a big win for shareholders in the short term, considering Mr. Musk's outsize role at the company. The stock should bounce back Monday, and it is possible the shares get a further boost when Tesla reports third-quarter deliveries later this week. If the company takes the governance overhaul seriously, Tesla has a chance to create a stronger organization in the long term as well.

However, the new chairman will have a lot of work to do, including reining in Mr. Musk's more problematic impulses, figuring out why senior executives keep leaving the company and helping install strong replacements. The entire board will have to perform better and clearly show its independence from Mr. Musk. The first test could occur in the coming months because Tesla will likely need to shore up its balance sheet by raising fresh capital.

Most importantly, Tesla needs to fix the capricious manner in which Mr. Musk runs his company, which is what caused trouble with regulators in the first place. There is reason to be skeptical he can do it. Just last Thursday, he called the SEC fraud lawsuit "unjustified" in a statement.

"Integrity is the most important value in my life and the facts will show I never compromised this in any way," he said, before settling fraud charges less than two days later.

Mr. Musk's poor judgment continued over the weekend when he emailed employees to say the company is "very close to achieving profitability" in the third quarter. While he has said in the past that the Tesla would earn a profit in the quarter, it wasn't a good idea to send an email like just as he was settling with the SEC for driving up the stock with his tweet about going private.

Great companies set realistic operational goals they can actually meet, don't disseminate material information via internal emails and don't taunt short sellers on social media. A first step toward winning back investor trust would be to issue realistic financial guidance for 2019. The lack of that information this late in 2018 is a curious omission for a company that plans to dominate the global automotive industry over the long term.

The SEC settlement closes an ugly chapter in Tesla's history. Monday should be a good day for the **stock price**, but the real work is only just beginning.

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THE WALL STREET JOURNAL.

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**Wall Street's Biggest Business Braces for Lackluster Third-Quarter Results; The volatility that has boosted banks' stock-trading business is hampering their fixed-income, commodities and currencies desks**

By Telis Demos
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30 September 2018
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The same **volatility** that has boosted banks' stock-trading business is hampering their fixed-income, commodities and currencies desks, setting Wall Street up for another tepid quarter.

The two biggest U.S. trading banks, JPMorgan Chase & Co. and Citigroup Inc., expect to report lukewarm results in their markets businesses for the third quarter. JPMorgan said this summer it anticipated a small decline from the year-ago period, while Citigroup said it might record a small uptick.

The threat of a trade war and increasing uncertainty about the inflation outlook have roiled stocks at times this year, giving a lift to traders dealing in stocks and derivatives tied to **volatility**. Yet the uncertainty has crimped some corporate activity, such as cross-border investment and debt issuance—major drivers of trading in interest rates, currencies and bonds.

Analysts expect that strong performances in stock-trading units will be erased by declines elsewhere. Susan Roth Katzke, an analyst at Credit Suisse Group AG, forecasts that fixed-income trading will log a year-over-year revenue decline of around 5% to 10% for the third quarter, even as equities revenue rises by as much as 5%.

Wall Street's fixed-income, currencies, and commodities businesses are still a shadow of what they were. In 2012, the dozen biggest banks globally generated some $100 billion in revenue from those desks, versus less than $70 billion last year, according to industry data tracker Coalition.

Until this year, revenues stemming from interest-rates and currencies trading had been a rare bright spot, rising from a low point in 2014. Banks have sought to reorient the business around corporate customers, which provide a steady stream of activity related to financing and trade.

Through the first half of this year, revenues in rates and foreign-exchange trading for U.S. banks fell 12% from 2017, according to figures from the Office of the Comptroller of the Currency. Rates and currencies make up more than 40% of banks' total trading revenue.

By contrast, stock-trading desks at big banks have been enjoying their best year in a decade. Across all banks, stock-trading revenue is up 21% so far this year, according to the OCC.

Wall Street doesn't appear ready to bet that the slowdown in rates and currencies trading will be an extended lull, as it was for years with stocks.

While the Federal Reserve said it expects to raise rates one more time this year, uncertainty over the longer-term outlook could drive trading activity. Additionally, a slowdown in central banks' buying of government bonds and an increase in U.S. debt issuance could spur bank clients to step up their purchasing of Treasurys and related derivatives.

Banks also are hesitant to scale back any services they provide to corporate clients of their trading desks, who can supply lucrative business to their investment and commercial banks.

"Banks are committed to the [trading] business because their clients are committed to the business," Credit Suisse's Ms. Katzke.

Assets on the balances sheets of the five biggest trading banks —JPMorgan, Citigroup, Bank of America Corp., Goldman Sachs Group Inc. and Morgan Stanley—related to the rates business at the end of June collectively stood at their highest level since the first quarter of 2014, according to figures compiled by Credit Suisse.

Another key measure, the value of derivative contracts held by U.S. banks tied to interest rates, also was up 13% from a year ago as of the end of the second quarter, according to the OCC.

"For the U.S. banks, we are back in an investment phase in the [trading] business, with the belief that these businesses have passed their trough," Ms. Katzke said.

A big risk, however, is that an unexpected change in inflation expectations or in forecasts of central banks' behavior could spark a rush to exit investments tied to rates, including U.S. Treasurys.

In that case, banks may find themselves exposed, according to Moody's Corp. A disorderly sale of Treasurys or a hiccup in global growth could impact banks' revenues through "market or credit losses and reduced client activity," the ratings firm said in a recent report.

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THE WALL STREET JOURNAL.

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**Dollar Loses Its Mojo; A confluence of factors have sent the greenback into reverse after a strong first-half rally**

By Ira Iosebashvili
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A dollar rally that has pressured everything from emerging markets to commodities in 2018 is reversing into the year's end.

The ICE Dollar Index, which measures the U.S. currency against a basket of six others, has given up around a third of its gains from the year's first eight months, falling 1.7% from its August peak.

A number of factors have dovetailed in recent months to weigh on the dollar. A gradual U.S. approach toward imposing tariffs on Chinese goods has sparked hopes that the U.S. and China may eventually resolve their trade dispute, encouraging investors to cut back on haven bets such as the dollar and shifting into U.S. shares and beaten-up emerging-markets currencies and stocks. That could pressure the dollar in coming months.

This trade conflict between the world's two largest economies had buoyed the greenback earlier in the year, with many investors believing the U.S. would be less damaged than other countries in an all-out trade war.

"Risky assets look a little bit more attractive and investors are looking to dip their toes back into other asset classes," said Mark McCormick, North American head of foreign exchange strategy at TD Securities.

The dollar also has been weighed down by signs of burgeoning growth outside the U.S. European Central Bank head Mario Draghi in September delivered an upbeat assessment of the region's economy and confirmed a plan, announced in June, to wrap up the ECB's €2.5 trillion ($2.91 trillion) bond-buying program by the end of the year. Meanwhile, Japan's economy returned to growth in the second quarter after a contraction in the first three months of the year.

At the same time, many investors already anticipate four interest-rate increases in 2018. The Federal Reserve raised rates for the third time this year in September and is widely expected to raise them once more in December. While tighter monetary policy in the U.S. typically makes the dollar more attractive to yield-seeking investors, some believe the market already has factored the next few rate increases into the currency's price.

Taken together, these factors have damped investor enthusiasm for the U.S. currency.

"We believe that dollar strength, based on macroeconomic and monetary-policy divergence, has almost run its course," analysts at the Wells Fargo Investment Institute wrote in a recent note to clients. They expect the dollar to remain flat against the euro for the remainder of 2018 and depreciate against the common currency next year.

A weaker U.S. currency would offer some relief to the battered currencies of emerging-markets countries where dollar strength has contributed to turmoil in recent months, such as Turkey, Argentina and South Africa. These nations, along with many other developing markets, accumulated large amounts of dollar-denominated external debt in recent years, which became more difficult to service when the dollar and U.S. yields rose earlier in 2018.

It would be less welcome in Europe and Japan, whose weaker currencies have helped fuel impressive economic rebounds. The ECB expects "a relatively vigorous pickup in underlying inflation," Mr. Draghi said in September. Weakness in the dollar can boost other currencies, such as the euro, smothering nascent inflation in the eurozone and other economies.

In the U.S., the dollar's downshift could ease pressure on multinational companies whose balance sheets have suffered because they need to convert foreign profits into the U.S. currency. It also could help buoy commodities such as oil, gold and copper, which are priced in the U.S. currency and become more affordable to foreign buyers when the dollar depreciates. **Oil prices** are up 17% from their mid-August lows, while copper prices have risen 9%.

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THE WALL STREET JOURNAL.

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**Reignited Rally Sets Off Talk of $100 Oil; Geopolitical risks, including looming sanctions on Iran, have pushed Brent price up 24% this year**

By Amrith Ramkumar
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**Oil prices** are again marching higher, prompting talk that crude could reach $100 a barrel for the first time since 2015's crash.

Brent crude, the global benchmark for **oil prices**, jumped 4.1% in the third quarter to $82.72 a barrel, the highest level in nearly four years. Brent's fifth consecutive quarterly advance marks its longest such streak since 2008. U.S. crude edged down from its most recent multiyear high, falling 1.2% to $73.25 a barrel last quarter, though it has risen in five of the past six weeks. Investors have grown more **bullish** ahead of Nov. 4, the U.S. sanctions deadline for companies to stop buying Iranian oil.

Sentiment was bolstered, too, by the recent decision of the Organization of the Petroleum Exporting Countries and its allies to leave production steady. That move, analysts said, convinced investors that the removal of Iranian oil from the market, along with supply disruptions in places such as Venezuela, will lead to large crude shortages.

The result: Brent is up 24% for the year so far and West Texas Intermediate, the U.S. gauge, has risen 21%.

"When you have a geopolitical risk backdrop like this, it just fuels **bullish** market sentiment," said Michael Cohen, head of energy commodities research at Barclays. "The fundamentals of the market are tightening before some had expected."

Further underpinning oil's rally is investor confidence that a robust U.S. economy will continue to keep fuel consumption near record levels. That belief has prompted calls for **oil prices** to reach $100 again, a level Brent hasn't hit since September 2014.

While Brent would have to rise another 21% to reach the $100 level, this isn't idle chatter: **Bullish** options that pay out if Brent hits $100 by January increased by more than 62% in the past week, Intercontinental Exchange data as of Sept. 27 by QuikStrike show.

Oil's rally is also luring speculators. Hedge funds have boosted net **bullish** bets on Brent for five consecutive weeks, pushing them to their highest level since May during the week ended Sept. 25, ICE data show.

Some analysts estimate that about one million barrels a day of Iran's roughly 2.5 million barrels a day of oil exports could ultimately be at risk from U.S. sanctions, removing more oil from the market after Iranian shipments have already been falling.

Saudi Arabia, the world's largest oil producer and de facto head of OPEC, has insisted it can fill any supply shortfall created by the Iran sanctions. But some analysts say recent increases in output from large suppliers and production disruptions have eroded global spare capacity, the production that can be quickly turned on in an emergency.

"Without spare capacity, OPEC is relatively impotent in relation to preventing rising prices," said Richard Robinson, manager of the Ashburton Global Energy Fund.

In the U.S., infrastructure bottlenecks due mainly to pipeline issues and worker shortages—particularly in prolific regions such as the Permian basin—have prevented production from rapidly growing, cutting off more supply from the broader market and leading to a nearly $10 gap between global and U.S. prices.

Traders also are bracing for a price surge that could cause a run-up in retail gasoline prices in the U.S.

How much pain there is at the pump could inject further uncertainty into the politics around oil, especially ahead of U.S. congressional midterm elections on Nov. 6. While President Trump in May announced that his administration would reinstate sanctions on Iran, the U.S. for months largely avoided the side effect of rising fuel costs, with **oil prices** flatlining this summer as Saudi Arabia and Russia increased production before turning up again.

Average American gasoline prices also have been largely steady after nearing $3 a gallon earlier this year, their highest level since 2014.

If gasoline prices leap, some analysts believe the Trump administration may come under political pressure to act, say by granting waivers to companies seeking to buy Iranian oil or dipping into the Strategic Petroleum Reserve, the country's emergency oil stockpiles. The latter has historically been viewed as a last-ditch option in an effort to contain price rises.

Should the conflict with Iran ramp up, "I don't see any barrier whatsoever for **oil prices** hitting $100 a barrel," said Matt Badiali, research analyst at investment research firm Banyan Hill Publishing. "Going into the holiday travel season, that would be really frustrating for the American consumer."

Aside from consumers, more expensive oil could threaten U.S. corporate profits and indirectly push prices for a variety of goods higher. If this stoked inflation, the Federal Reserve could feel pressure to quicken its pace of interest-rate increases.

Of course, the oil market is notoriously **volatile**. Some investors expect higher production from Saudi Arabia and Russia to eventually cool the current rally—something that happened this summer after a June rise in prices.

Markets around the world also have largely shrugged off the risk of an escalation in the U.S.-China trade dispute, which could crimp global growth and hurt demand for crude.

So moves on trade that either intensify or cool the dispute also could influence where oil heads into the end of the year.

"I don't think anybody can anticipate how this all plays out in the next two months," said Barclays' Mr. Cohen.

Christopher Alessi and Gunjan Banerji contributed to this article.

Write to Amrith Ramkumar at amrith.ramkumar@wsj.com

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International New York Times

business
**China Censors Bad Economic News Amid Signs of Slower Growth**

By SUI-LEE WEE and LI YUAN
1,076 words
30 September 2018
International New York Times
INHT
English


BEIJING — China has long made it clear that reporting on politics, civil society and sensitive historical events is forbidden. Increasingly, it wants to keep negative news about the economy under control, too.

A government directive sent to journalists in China on Friday named six economic topics to be "managed," according to a copy of the order that was reviewed by The New York Times.

The list of topics includes:

■ Worse-than-expected data that could show the economy is slowing. ■ Local government debt risks. ■ The impact of the trade war with the United States. ■ Signs of declining consumer confidence■ The risks of stagflation, or rising prices coupled with slowing economic growth ■ "Hot-button issues to show the difficulties of people's lives."

The government's new directive betrays a mounting anxiety among Chinese leaders that the country could be heading into a growing economic slump. Even before the trade war between the United States and China, residents of the world's second-largest economy were showing signs of keeping a tight grip on their wallets. Industrial profit growth has slowed for four consecutive months, and China's **stock market** is near its lowest level in four years.

"It's possible that the situation is more serious than previously thought or that they want to prevent a panic," said Zhang Ming, a retired political science professor from Renmin University in Beijing.

Mr. Zhang said the effect of the expanded censorship strategy could more readily cause people to believe rumors about the economy. "They are worried about chaos," he added. "But in barring the media from reporting, things may get more chaotic."

The directive didn't appear to affect run-of-mill daily coverage of economic data, which could still be widely found online in China on Friday. Instead, the directive appeared to be aimed at easing the overall tone.

Indeed, another notice sent on Friday instructed online news outlets to remove comments at the bottom of news articles that "bad-mouth the Chinese economy."

These topics pertain to "China's economic downturn," "China's stagflation," "new refugees," "consumption downgrading" and "other harmful remarks that criticize the development prospects of China," according to a copy of the notice reviewed by The Times. Consumption downgrading refers to Chinese consumers looking for ways to spend less.

China's propaganda department couldn't be reached late Friday for comment.

Negative economic news could undermine the careful message Chinese officials have tried to transmit to the public in recent months. They have said that the country's vast and growing ranks of consumers, as well as China's increasing sophistication in technology and other areas, would help it weather any ill effects from rising American tariffs.

At the same time, officials have made moves to juice the economy. The government has loosened restrictions on big but costly local government projects like subways and light rail lines. It has also promised tax cuts for businesses and other efforts to generate more construction.

The trade war could certainly worsen the economic climate if it lingers, leading to job losses and even weaker consumer sentiment. But China has more deep-seated economic problems.

Officials are trying to clean up huge debts accumulated by local governments. Curbing debt could mean slower economic growth, as it deprives borrowers of the funds they would otherwise spend.

China has long maintained a tight grip on the media, though the economy traditionally has been one of the freer domains of reporting. Even after China began more closely managing its economic message following market turmoil in 2015, aggressive journalists have covered the fallout of peer-to-peer online lending schemes and the problems posed by local government debt, among other issues.

On paper, China's gross domestic product, its main economic figure, indicates smooth sailing. But the figure is widely doubted, and many economists are forecasting a slowdown to varying degrees.

Mark Williams, chief Asia economist of Capital Economics, said the firm expects the Chinese economy to slow down to 5 to 5.5 percent from 6.9 percent last year. Despite the lower forecast, he stressed that it was "not a weak number" for the Chinese economy.

"One of the problems is there's a lot of doubt about official Chinese data," Mr. Williams said. "And when they come out with these directives, it just raises more questions."

In the past year, domestic news media have had to write their stories on the economy with a gentler tone, said a journalist covering finance for a Chinese business newspaper, who asked not to be named because of the sensitivity of the matter.

Censors have also erased online commentary that contained the phrases "consumption downgrade," taxes, debt and unemployment, according to the Journalism and Media Studies Center at the University of Hong Kong, which monitors censorship on Weibo, China's Twitter-like social media service.

One post that was removed by censors said: "The bad news in the market is exploding, pessimistic viewpoints are spreading, many retail investors are in despair."

Another read: "Will the emergence of robots free up labor or cause unemployment and poverty?"

The scrutiny over economic news adds to a broader pattern of the tightening of control over media since President Xi Jinping came into power in 2012. Particularly online, the Chinese government has centralized and beefed up regulatory agencies that monitor content. Recently, the agencies have come down harder on entertainment news and celebrity gossip, in addition to political and social issues.

On Wednesday, Phoenix News Media, a Hong Kong-based outlet with big operations in mainland China, said the Chinese authorities had instructed it to "rectify" its news portal, ifeng.com. The Cyberspace Administration of China, the country's main internet regulator, said that Phoenix had "disseminated illegal and harmful information, distorted news headlines and shared news information in violation of rules."

Two weeks earlier, NetEase, an online news portal, said it had to suspend updating its financial platform "because of serious problems."

Sui-Lee Wee reported from Beijing, and Li Yuan from Hong Kong

PHOTO: Watching the markets in Shanghai. The government's directive betrays a mounting anxiety among Chinese leaders of a slump. (PHOTOGRAPH BY JOHANNES EISELE/AGENCE FRANCE-PRESSE — GETTY IMAGES) (B3)

* Trump Hits China With Tariffs on $200 Billion in Goods, Escalating Trade War

* China's Strong Economic Growth Figures Belie Signs of Weakness

Document INHT000020180930ee9u00005

 

THE WALL STREET JOURNAL.

World

**Saudi Arabia Plans More Spending to Boost Sluggish Growth; The approach is part of an ambitious transformation plan to wean the kingdom's economy away from oil**

By Donna Abdulaziz in Jeddah and Rory Jones in Dubai
840 words
30 September 2018
12:04 PM
The Wall Street Journal Online
WSJO
English


Saudi Arabia said Sunday it intends to significantly increase spending next year as it benefits from higher **oil prices**, a plan that will help boost sluggish growth and create more jobs in the Middle East's biggest economy.

The government's budget spending is expected to reach more than 1.1 trillion Saudi riyals ($295 billion) in 2019, about 7% higher than projected expenditure for this fiscal year, the Saudi ministry of finance said in a brief pre-budget statement. It usually issues a more detailed annual budget statement in December.

The kingdom, under Crown Prince Mohammed bin Salman, is carrying out an ambitious transformation plan to wean its economy away from oil by boosting the private sector. But growth slowed as it cut back on spending, including on subsidies, to cope with the sharp fall in the price of oil since 2014. Energy sales account for more than 70% of Saudi Arabia's budget revenue.

It isn't clear if Saudi Arabia will roll back some of its reform plans with **oil prices** now back up. An increase in spending will help boost growth, which will make it easier for the government to roll out the tough economic changes needed in the longer term, some analysts say.

Saudi Arabia is reluctant to see a significant fall in the price of oil as such a scenario would drive down revenues, expand its budget deficit and constrain its ability to implement reforms that it hopes will diversify the economy.

The finance ministry said it expects the kingdom's gross domestic product, which contracted in 2017, to expand by 2.3% next year and improve gradually to reach 2.4% in 2021 as a result of the country's economic reforms. The International Monetary Fund expects the economy to grow 1.9% this year, with the non-oil sector forecast to strengthen 2.3%.

Finance Minister Mohammed Al-Jadaan said the main thrust of the government in the 2019 budget is the continued implementation of the kingdom's transformation plan, called Vision 2030, which includes diversification of the economy, boosting non-oil revenue and achieving fiscal balance by 2023.

The government expects revenues to increase by 11% to 978 billion riyals next year, the finance ministry said, which means it would again run a fiscal deficit to implement spending. It plans to finance that budget deficit with debt issuances in the capital markets, after raising more than $50 billion in the past three years. The government expects debt to reach about 22% of GDP in 2019 and grow to about 25% in 2021.

"Government spending has the biggest impact on GDP," said Mazen al-Sudairi, head of research at Riyadh-based Al Rajhi Capital. "It will create more investments and therefore more jobs for Saudis."

Unemployment among Saudis stands at nearly 13% according to latest government issued statistics. Saudi Arabia is attempting to reduce this unemployment rate through initiatives such as levies on firms that employ expatriate workers and by enforcing stricter nationalization quotas in the private sector. But the efforts have so far had mixed success.

Saudi Arabia's finances are being closely watched in Washington. President Donald Trump has repeatedly called on Saudi Arabia, as the de facto leader of the OPEC oil cartel, to lower prices so that Americans see cheaper fuel costs. The issue has become particularly acute for the Republican White House ahead of crucial midterm elections in November when the Democrats are expected to make gains in Congress.

The U.S. leader on Saturday spoke with Saudi Arabia's King Salman, discussing the oil market and the need to maintain supplies to ensure global economic growth, according to a statement from the official Saudi Press Agency.

**Oil prices** crashed in 2014 but have since recovered to trade at about $80 a barrel after Riyadh-led OPEC and other nations agreed last year to limit supply.

At a meeting last week in Algiers, OPEC decided not to increase supply, even as Iranian oil shipments are expected to fall, as the cartel members fear a glut would again drag prices down.

The government in December announced a record fiscal stimulus to boost the economy after a period of austerity in the wake of the 2014 **oil-price** collapse. It had used cuts to infrastructure projects and government employee benefits to tighten a budget deficit that mushroomed to about 15% of gross domestic product in 2015.

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Related Reading

* Saudi Arabia's Economic Revamp Means More Jobs for Saudis—If Only They Wanted Them (June 19)

* Saudi Arabia to Spend Billions to Revive Foreign Investment (July 22)

* Saudi Arabia Pressures Aramco to Take On Debt After IPO Stalls (July 26)

* Saudi Arabia's Spat With Canada Risks Backlash From Investors (Aug. 6)

Document WSJO000020180930ee9u001b9

 

THE WALL STREET JOURNAL.

Economy

**Consumers Drive the Economy, Stock Market Higher; The next snapshot of the U.S. consumer comes on Friday, when the Labor Department releases data on unemployment, wages and jobs growth**

By Jessica Menton and Akane Otani
294 words
30 September 2018
11:00 AM
The Wall Street Journal Online
WSJO
English


The American consumer appears to be in good shape heading into the final quarter of the year, which includes the busy holiday-shopping season. Investors will be watching Friday's jobs report for further evidence the U.S. economy can keep humming into 2019.

Consumer confidence climbed to an 18-year high in September, supported by a strong labor market. Analysts will get their next snapshot of the U.S. consumer on Friday, when the Labor Department releases fresh data on unemployment, wages and jobs growth.

Consumer spending, which accounts for more than two-thirds of the U.S. economy, cooled in August, though economists still expect strong growth in the final stretch of the year. Consumer savings matched July's pace.

Discretionary stocks are outperforming the broader U.S. **stock market**, signaling consumers are confident in the heath of the economy and willing to part with their disposable income.

Online retail giant Amazon.com has soared this year thanks to a boom in sales. But more traditional retailers selling goods ranging from sportswear to home accessories have also thrived.

Still, within the consumer discretionary sector, department stores and companies selling textiles, apparel and luxury goods have raced past retailers in the automobiles and household durables space.

Many investors are optimistic that the U.S. consumer will keep supporting economic growth. Yet some warn that if **oil prices** keep rising, it could dent spending further down the line.

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THE WALL STREET JOURNAL.

Markets

**Investors Say They Were Harmed by Manipulation in Volatility Products; A complaint alleges that market players consistently manipulated prices of derivatives tied to the VIX**

By Gunjan Banerji
579 words
29 September 2018
09:56 AM
The Wall Street Journal Online
WSJO
English


A group of investors filed a complaint against Cboe Global Markets Inc. on Friday, alleging that they experienced losses because its popular **volatility** products were manipulated.

The complaint alleges that market players consistently manipulated prices of derivatives tied to the VIX—a widely watched **volatility** measure that is also known as the Cboe **Volatility** Index. The investors claim that Cboe, which operates the largest options exchange in the U.S., knew about the activity, according to the complaint filed in the Northern District of Illinois. The proposed class-action lawsuit needs a judge's ruling in order to proceed.

"Cboe designed, then regularly administered for profit, a fatally flawed process," the lawsuit says. "As a result of CBOE's malfeasance, the prices for VIX options and VIX futures have been subject to wholesale manipulation."

A spokeswoman for Cboe declined to comment on the complaint. The Chicago-based company has previously said that trading alleged as irregular is consistent with normal activity and not evidence of manipulation. It has also previously said it regularly monitors for nefarious activity and takes disciplinary action when warranted.

The VIX is calculated using options prices on the **S&P 500 index**. It tends to rise when stock prices fall and has hence become a popular way for investors to hedge other holdings or bet on future turbulence in the market. A whole ecosystem of products that allow investors to wager on the VIX has emerged, including futures and options contracts that have turned into a lucrative business for Cboe.

But claims that the VIX is manipulated have cropped up in recent years. And the gauge became the center of widespread attention in February when two exchange-traded products tied to it collapsed.

In recent years, as share prices continuously rose, some of the ETPs, which trade like stocks, had become a way for investors to bet **volatility** would stay low—known in the market as the "short vol" trade. That came to a head in February as **volatility** spiked in U.S. equities, triggering losses for "short vol" investors across Wall Street and Main Street.

In the lawsuit filed Friday, investors take issue with a regular auction operated by Cboe, which determines the prices of VIX futures. The investors allege they were harmed when the auction distorted trading and made the prices of VIX futures and options "artificial."

The complaint also claims price tampering of such derivatives affected trading of the VIX ETPs.

Some in the options industry have told The Wall Street Journal that unusual activity in the monthly auction could be driven by investor hedging as opposed to any nefarious activity.

Cboe has made moves to change its monthly auction to boost trading since February.The exchange operator has tried to reduce some of the anomalous pricing that has occurred on days VIX futures contracts expire. Cboe recently filed a proposal with the Securities and Exchange Commission to make changes to the auction. The proposal requires regulatory approval.

Cboe shares were once thought of as a beneficiary of higher **volatility**, since turbulence in markets could lead to more trading of its products. But the once highflying stock is down 23% in 2018, even as shares of other exchange-operators have rallied this year.

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THE WALL STREET JOURNAL.

Markets

**Europe Is Left in the Dust as U.S. Stocks Roar; While U.S. and Japanese shares raced ahead, Europe's shares were left behind in third quarter**

By Riva Gold
828 words
29 September 2018
07:00 AM
The Wall Street Journal Online
WSJO
English


European stocks have been left behind by a rally that has taken the U.S. market to record highs in the third quarter.

Few analysts see the region catching up soon, unless there is clarity on the political and trade concerns that pushed investors to sell.

Investors have withdrawn money from European equity funds in 28 of the past 29 weeks, driving the share of Europe in global portfolios to its lowest since January 2015, when the European Central Bank announced its massive bond-purchase program, according to data from fund tracker EPFR and the Institute of International Finance.

That has largely reversed the tide of cash that poured into the region in early 2017, when an election in France elevated investors' preferred candidate to power. In contrast, funds in the U.S., Japan and even some emerging-market equities have drawn inflows this year.

The Stoxx Europe 600 index rose less than 1% in the third quarter, compared with a 7.2% gain for the **S&P 500** and 8.1% for Japan's Nikkei Stock Average. The European index is now trading below where it was one year ago, compared with an 8.2% gain in a broad index of world stocks.

"U.S. client interest in Europe is very low right now—almost as low as it gets," said Richard Turnill, BlackRock's global chief investment strategist.

As the U.S. economy continues its robust run, the gap between 10-year German and U.S. government bond yields has reached its widest since the euro was launched in 1999, according to data from Tradeweb and Thomson Reuters.

The downbeat sentiment comes even as Europe's earnings expectations for the year have remained stable, the euro and British pound have stopped climbing, and the region's economy has shown signs of stabilizing after a tricky start.

"Our view on Europe is predominantly politically driven," said Candice Bangsund, portfolio manager at Fiera Capital, which currently holds a smaller-than-usual allocation to European stocks.

The future trading relationship between the U.K., one of the region's largest economies, and the rest of the continent remains uncertain as Brexit negotiations drag on. Italy's new government, meanwhile, has significantly widened its budget-deficit target, raising questions about the country's debt sustainability and relationship with Brussels.

The U.K. and Italy's benchmark stock indexes have both seen double-digit percentage falls in their price-to-earnings ratios this year amid the uncertainty.

European companies are also more exposed than those in the U.S. to emerging markets, and the developing world has been hit by a rising dollar, expensive oil and concerns about trade protectionism.

Roughly 19% of revenues from companies listed in the Stoxx Europe 600 come from emerging markets, according to FactSet. That compares with 14% for the **S&P 500**, an index of large-cap U.S. stocks.

Roland Kaloyan, head of European equity strategy at Société Générale, said the correlations between European stocks and emerging markets recently reached levels last seen in 2010.

But trade protectionism is by far the biggest risk to Europe's outlook, analysts say.

Europe's auto sector has been hit particularly hard by worries about tariffs, trading down about 23% from its peak in January.

"Europe is more exposed to protectionism because it has a more open economy and has closer ties to China," said Silvia Dall'Angelo, senior economist at Hermes Investment Management.

Uncertainty about future trade relations has already hit eurozone exports. In manufacturing, export orders failed to grow for the first time in five years.

All this means there will be bargains in Europe, should more clarity come on the political front, some investors say.

European stocks now trade at 13.9 times future expected earnings, compared with 15 at the start of the year.

European companies are seeing revenue upgrades for the first time in a year, according to strategists at UBS. "A lot of investors are looking at valuations and looking for a reason to come back" to Europe, said Mr. Kaloyan. "If we got some sort of clarity on Italy or Brexit, we could see a rebound."

Much will also depend on whether investors continue to favor so-called growth stocks such as technology companies, which make up a small portion of European indexes. Tech stocks in the **S&P 500** are up roughly 19% this year and now make up 21% of that index. Tech makes up just 5% of the Stoxx Europe 600. Unless value stocks—those that are trading for the lowest prices relative to their earnings or underlying net worth—start to outperform, it will be difficult for Europe to pull ahead, fund managers say.

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THE WALL STREET JOURNAL.

Markets
**REITs Wrestle With Rising Interest Rates; After a strong second quarter, real-estate investment trusts slipped during the third quarter**

By Mengqi Sun
630 words
29 September 2018
12:00 PM
The Wall Street Journal Online
WSJO
English


Rising interest rates are taking a toll on U.S. REITs.

After a strong second quarter in which they beat the **S&P 500** by close to 6 percentage points, real-estate investment trusts in the third quarter fell behind again.

In the third quarter, the FTSE Nareit All Equity REITs Index gained 0.5%, compared with a 7.6% return for **S&P 500** over the same period.

Despite the uptick in the second quarter, the return of the REITs Index has trailed behind **S&P 500** by more than 7 percentage points for the first three quarters this year.

Investors have lost some enthusiasm too. About $14.8 billion flowed out of U.S. REIT mutual funds through the end of August this year, up from $13.4 billion in 2017, according to Green Street Advisors.

This past week, as the Federal Reserve lifted short-term interest rates on Wednesday, analysts are divided over the future performance of REITs.

S&P Global Ratings credit analysts find that higher interest rates don't pose a big problem solely for U.S. REITs, as their debt structures mostly consist of fixed-rate debt, rather than variable-rate debt, according to a report published on Monday.

But James Sullivan, head of real-estate research at BTIG LLC., said the weakness of bonds prices—as the yields get higher—would provide another headwind for U.S. REITs.

"For the investors who can buy any securities, they're going to have a tough time to overweight REITs," Mr. Sullivan said.

Within REITs, the lodging and resorts sector turned in one of the highest returns during the first nine months this year at 9.6%, according to data provided by FTSE and Nareit.

This was largely due to strong corporate earnings that tend to drive up business travel, said Cedrik Lachance, director of REIT research at real-estate research firm Green Street Advisors.

"The economy is doing a lot better than expected in the first nine months; it's no surprise that lodging has performed well so far this year," he said.

With robust growth in e-commerce continuing, the demand for warehouses keeps rising. Industrial REITs have been one of the strongest performing sectors for years and had a 2018 total return of 7.4% by the end of September.

"There is a long-term growth story that is embedded into the industrial space," said Karin Ford, an analyst at MUFG Securities, noting that "there is a very resilient demand" in the sector from institutional investors.

The retail sector had a strong second quarter. For instance, strip-shopping centers REITs turned in an 8.3% return for the month of June. But the overall sector has been down slightly so far this year.

The self-storage sector also lost most of its gain from the second quarter with a 10% quarterly drop. The most likely culprit, according to Mr. Lachance, is earlier strong demand that attracted more competition through new developers.

The strong performance in REITs in the second quarter was also aided by mergers-and-acquisitions activity. Eight deals for REITs, totaling $16.5 billion, were announced between April and June, in addition to the two announced deals of $4.4 billion in the first quarter this year.

A bright spot could come from apartment REITs, analysts said. The sector had a total return of 5.4% for the first nine months, and could benefit from continuing demand to rent and a slowdown in supply.

"It's going to improve fundamentals and growth," said Ms. Ford. "I don't think the market has fully priced that in today."

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THE WALL STREET JOURNAL.

Markets
**Greenback Weighs On Corporate Profits; Dollar's strength a drag on multinationals that record much of their revenues overseas**

By Michael Wursthorn
982 words
29 September 2018
12:00 PM
The Wall Street Journal Online
WSJO
English


The U.S. dollar's surge this year is likely to dent third-quarter earnings at big multinational corporations and stir consternation in a **stock market** that is already grappling with trade tensions and higher interest rates.

The greenback has risen 4.3% against a basket of 16 other currencies in 2018, even after growth slowed in the latest quarter to 1.9%. The stronger dollar makes converting foreign profits into the U.S. currency more expensive, dragging earnings lower at dozens of companies including Johnson & JohnsonNike Inc. and Goodyear Tire & Rubber Co.

Although companies in the **S&P 500** are expected to report another period of double-digit profit growth, more firms are issuing warnings ahead of earnings season—and currency fluctuations are one of the primary factors to blame. About 76% of the 98 companies that have given projections have issued negative guidance, which is above the five-year average, according to FactSet.

Overall, profits are expected to increase 19% from a year earlier in the third quarter, marking a slowdown from the 25% growth notched in the first and second quarters, according to the data provider. Robust corporate earnings have helped propel U.S. stocks to record highs this month, but concerns about peaking profits, along with ongoing trade tensions and monetary tightening by the Federal Reserve, have spooked investors for much of the year.

"The move in currencies has been underappreciated," said James Tierney, a portfolio manager with AllianceBernstein. "The dollar's rise and the moves in developing-market currencies have truly been staggering, especially for companies with huge exposure to India, Latin America and Asia."

Online auction house eBay Inc. warned over the summer that the dollar's strength would likely knock $150 million off its revenue for the year, while Johnson & Johnson has said the currency's jump forced it to trim its revenue projections and narrow its earnings estimate.

Athletic apparel powerhouse Nike, which reported its latest quarterly earnings Tuesday, said the dollar has been a "slight headwind" over the past three months and will curtail revenue growth for the year.

Nike got roughly 65% of its revenue from overseas last year, with China and Canada among the biggest foreign markets for the maker of sneakers and sportswear, according to FactSet.

Many companies attempt to limit the impact of currency swings through hedging programs. Nike Chief Financial Officer Andrew Campion, for instance, said this week on a conference call with analysts that the company's hedging program delays the impact of foreign-exchange movements on its profitability for 12 to as many as 24 months.

But the program, as well as those run by some other companies, tends to hedge for developed-market currencies, such as the euro, and not emerging markets. Many of those countries service their debt using the greenback, making them more economically sensitive to the dollar's moves. Nike said it isn't "economical" to hedge for currency risks in countries like Turkey, Argentina and Brazil, and its exposure in China is only partially hedged.

At Goodyear Tire & Rubber, the dollar's gains against the lira, Brazilian real, yuan and the euro have been punishing this year. The tire maker warned over the summer that the dollar's ascent against those currencies will sap $60 million from its operating income for the year. That's on top of a projected $70 million shortfall due to softening market conditions in China.

With a foreign revenue exposure of roughly 56%, Goodyear Chief Executive Richard Kramer warned at a Morgan Stanley conference earlier this month that the translation effects of converting those overseas earnings into dollars have been having a "big impact."

Clorox Co., the maker of home-care and personal products from Glad trash bags to Burt's Bees lip balm, attributed the previous quarter's 2% drop in international sales to the devaluation of the Argentine peso.

The currency headaches are expected to continue and shave 2% from its total sales in fiscal 2019, Chief Financial Officer Kevin Jacobsen said at a Barclays consumer-staples conference this month.

Although the dollar has given up some of its gains in recent weeks as the euro and Japanese yen strengthened, several factors could propel the U.S. currency higher over the next several months.

The dollar could rise if the U.S. economy continues to grow at a rapid pace in line with the second quarter's 4.1% gross-domestic-product reading, said Peter Wilson, global fixed-income strategist at Wells Fargo Investment Institute, in a recent note.

Renewed trade tensions could also support another leg of the dollar's rally. Although most investors agree tariffs would be a drag across much of the economy, the U.S. is expected to better withstand a sharp escalation in the trade spat than other countries, such as China.

And rising interest rates could make the dollar more attractive to investors who are searching for higher-yielding investments. The Federal Reserve proceeded with its third rate increase in 2018 this week and has plans for one more this year and another four in 2019.

Still, Mr. Wilson and other analysts are wary of giving a near-term outlook given the uncertainty, but most agree that the dollar should be able to ride out the rest of the year relatively strongly before giving up some of those gains in 2019. And the dollar's ongoing strength could continue to beleaguer executives of multinational corporations.

"We now expect a relatively flat profile for the dollar versus the euro from now until year-end," wrote Mr. Wilson, but he added that the currency's situation remains "finely poised at the moment, with risks in both directions."

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THE WALL STREET JOURNAL.
U.S. EDITION

**EXCHANGE --- Heard on the Street: A Tricky Time for Inflation in China --- Surge in food costs is an unwelcome distraction**

By Nathaniel Taplin
476 words
29 September 2018
The Wall Street Journal
J
B12
English


[Financial Analysis and Commentary]

Summer in Beijing is already well in the rearview, but there's some unwelcome heat in the economy: Inflation, long dormant, is showing signs of revival.

That could complicate Beijing's effort to prosecute its trade conflict with the U.S. It could also make it far harder to arrest an investment slowdown that threatens to drag growth lower just as the Trump administration ratchets up the pressure on trade.

Faster consumer-price inflation in China is worrying for two reasons. First, unlike last year, it comes as economic activity is trending sideways or downward. The labor market is holding up for now, but higher prices could derail a nascent rebound in domestic consumption growth, which accelerated again in the second quarter after more than a year of weakening.

Second, inflation is affecting politically sensitive food prices, while last year rising service prices were the main driver. The uptick is also quite broad-based: In addition to food, prices for shelter, consumer goods, transportation and services have all risen noticeably faster since midyear. That suggests the cause goes deeper than temporary supply disruptions from bad weather and a swine fever outbreak. Core consumer inflation, which excludes **volatile** food and energy prices, ticked up in August for the first time since last September, excluding the Lunar New Year period, whose shifting dates make year-over-year comparisons difficult.

Headline inflation, at 2.3%, remains well below Beijing's 3% target. And the impact from trade tensions has so far been manageable: Despite big tariffs on U.S. soybeans, for example, rural soymeal prices are only about 7% higher than they were a year ago, according to Ministry of Agriculture data.

But the view ahead looks rockier. **Oil prices** just notched a post-2014 high -- the inflationary impact magnified by the yuan's big fall -- with little prospect of relief, given the looming Iran sanctions. And Beijing's campaign to prop up inefficient state-owned industrial companies at the expense of private competitors isn't likely to help, as higher upstream prices for basic industrial goods do eventually trickle down.

Add in bubbly housing prices, a hawkish Fed and the likelihood of a bigger tariff impact on soy prices later this year as inventories run down, further substantial monetary easing by Beijing would carry significant risk of more-serious inflation and an even weaker yuan.

But the alternative is just as unpalatable, risking a sharper investment slowdown and defaults at local governments' fundraising companies, which could roil the bond market.

Either way, 2019 looks like a tricky year for China even without a full-scale trade war waiting in the wings.


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The New York Times

The Upshot

**The Most Important Least-Noticed Economic Event of the Decade**

By Neil Irwin
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English


Sometimes the most important economic events announce themselves with huge front-page headlines, **stock market** collapses and frantic intervention by government officials.

Other times, a hard-to-explain confluence of forces has enormous economic implications, yet comes and goes without most people even being aware of it.

In 2015 and 2016, the United States experienced the second type of event.

There was a sharp slowdown in business investment, caused by an interrelated weakening in emerging markets, a drop in the price of oil and other commodities, and a run-up in the value of the dollar.

The pain was confined mostly to the energy and agricultural sectors and to the portions of the manufacturing economy that supply them with equipment. Overall economic growth slowed but remained in positive territory. The national unemployment rate kept falling. Anyone who didn't work in energy, agriculture or manufacturing could be forgiven for not noticing it at all.

Yet understanding this slump — think of it as a mini-recession — is important in many ways.

It helps explains the economic growth spurt of the last two years. The end of the mini-recession in the spring of 2016 created a capital spending rebound that began in mid-2016, and it has contributed to speedier growth since. **Oil prices** have reached four-year highs, a major factor in a surge in business investment this year.

It helps explain some of the economic discontent evident in manufacturing-heavy areas during the 2016 elections. It offers warnings for where the next downturn might come from, and shows how important it is for policymakers to remain watchful and flexible about unpredictable shifts in the global economy.

Most important, the mini-recession of 2015-16 offers a cautionary tale for any policymaker who might want to think of the United States as an economic island.

The episode is stark evidence of the risk the Trump administration faces in threatening economic damage to negotiate leverage with other nations on trade and security. What happens overseas can return to American shores faster and more powerfully than once seemed possible.

How it happened

The mini-recession defies neatness. It's a story of spillovers and feedback loops and unintended consequences. But here's a summary:

In 2015, Chinese leaders were concerned that their economy was experiencing a credit bubble, and they began imposing policies to restrain growth. These worked too well and caused a steep slowdown. That in turn caused troubles in other emerging nations for whom China was a major customer.

Meanwhile, the Federal Reserve, finally growing confident that the United States economy was returning to health, made plans to end its era of ultra-easy monetary policy.

As the Fed moved toward tighter money, its counterparts at the European Central Bank and the Bank of Japan were going in the opposite direction. The prospect of higher interest rates in the United States and lower rates in the eurozone and Japan fueled a steep rise in the value of the dollar on global currency markets.

That in turn made China's problems worse. China had long pegged the value of its currency to the dollar, so a stronger dollar was also making Chinese companies less competitive globally. When China attempted to reduce this burden by loosening the peg in August 2015, it faced capital outflows, making the economic situation worse.

Moreover, across major emerging markets, many companies and banks had borrowed money in dollars, so a stronger dollar made their debt burdens more onerous.

Put it all together, and when the Fed moved toward raising interest rates — as it eventually did in December 2015 — it was essentially making financial conditions tighter and therefore slowing growth across big swaths of the world.

The slowdown across emerging markets, in turn, meant less demand for oil and many other commodities. That helped cause their prices to fall. The price of a barrel of West Texas Intermediate crude oil fell to under $30 in February 2016 from around $106 in June 2014. The drops in the prices of metals like copper and aluminum, and agricultural products like corn and soybeans, were also steep.

That only heightened the economic pain for the many emerging economies that are major commodity producers, such as Brazil, Mexico and Indonesia.

Given falling prices and high debt loads among energy producers in the United States, the markets for stocks and riskier corporate bonds came under stress, especially in early 2016. That generated losses for investors and fears about the overall stability of the financial system.

Each of these forces has connections to the others. It wasn't one problem, but an intersection of a bunch of them. That made it devilishly hard to diagnose, let alone to fix, even for the people whose job was to do just that.

The view from Washington

When Federal Reserve officials meet eight times a year to set interest rate policy, their job, assigned by Congress, is to figure out what is best for the United States economy. Their job isn't to set a policy that will be best for China or Brazil or Indonesia.

Entering 2015, things were looking pretty good for the United States.

Inflation was below the 2 percent level the Fed aims for, but the traditional economic models on which the central bankers had long relied predicted that it would start to rise thanks to a rapidly falling unemployment rate.

Even when prices for oil and other commodities started falling in the middle of the year, the Fed's models viewed it as a positive for the overall economy. Sure, some oil drillers and farmers might experience lower incomes, but consumers everywhere would enjoy cheaper gasoline and grocery bills.

Although officials spent a lot of time monitoring the global economy, the fact remained that the United States wasn't as dependent on exports as many smaller countries. The 2008 financial crisis had shown how the American and European banking systems were deeply intertwined, but the same couldn't be said of the ties with Chinese banks.

In other words, through the summer of 2015 it sure looked to many Fed officials as if the sound move was to start raising interest rates.

At the Treasury Department, which is responsible for the United States' currency policies, it seemed well into 2015 that the strengthening dollar was mostly benign.

"There was a sense that the U.S. was doing well and the rest of the world was not doing very well," said Nathan Sheets, a Treasury under secretary at the time and now chief economist at PGIM Fixed Income. "It was driven by strong U.S. fundamentals."

But in late summer 2015, **financial markets** started to react more violently to the feedback loop of global currencies and commodities. It started to seem as if some of the old rules of thumb — about how a rising dollar or falling **oil prices** might affect the economy — might not apply.

 

Perhaps the economics models used by forecasters had become outdated, failing to fully account for the ways surging energy production had become more intertwined with the manufacturing sector and the **financial markets**.

“These things were all interconnected in different ways, and they all cycled back on the same industries and parts of the economy,” said Jay Shambaugh, a member of the Obama White House Council of Economic Advisers at the time. Still, distilling that complex story into crisp memos for senior officials was no easy task.

“You have to make memos short and to the point in the White House, and it was hard to say what exactly we thought was happening,” he said.

Behind closed doors at the Fed, officials started debating whether this outburst of **volatility** in markets really posed a risk to the overall economy. Should they stick to their plans to raise interest rates steadily, or slow down?

Over two days in October, the debate played out publicly.

Stan Fischer, the vice chairman of the Fed, was reluctant to adjust the planned rate increases, not wishing to let swings in **financial markets** dictate policy.

“We do not currently anticipate that the effects of these recent developments on the U.S. economy will prove to be large enough to have a significant effect on the path for policy,” he said in a speech in Lima, Peru, on Oct. 11, 2015.

Lael Brainard, a Federal Reserve governor who had worked on international issues at the Treasury, was quite a bit more worried.

“There is a risk that the intensification of international cross currents could weigh more heavily on U.S. demand directly, or that the anticipation of a sharper divergence in U.S. policy could impose restraint through additional tightening of financial conditions,” she said on Oct. 12 in Washington.

Ms. Brainard was right.

How the damage played out

The vicious circle of a stronger dollar, weaker emerging market growth and lower commodity prices caused spending on certain types of capital goods to plummet starting in mid-2015.

Spending on agricultural machinery in 2016 fell 38 percent from 2014 levels; for petroleum and natural gas structures — think oil drilling rigs — the number was down a whopping 60 percent.

The oil and gas exploration boom tied to fracking technology came to a halt with energy prices at rock-bottom levels, and with it sales of equipment tied to that boom.

With the fall in domestic capital investment in those industries and with weakness overseas, companies in related industries took it on the chin. Caterpillar, the maker of heavy equipment, had 30 percent lower revenue in 2016 than 2014.

In large segments of the economy, by contrast, it was business as usual. Business spending on investments like computers and office buildings kept rising, as did consumer spending.

Still, the industrial sector downturn was powerful enough to turn a strong expansion into a weak one. Overall growth fell to 1.3 percent in the four quarters ended in mid-2016, from 3.4 percent in the preceding year.

The national economy kept adding jobs. But Harris County, Tex., which encompasses energy-centric Houston and its near suburbs, shed 0.8 percent of its jobs in that span. In Peoria, Ill., hometown of Caterpillar, employment fell 3.2 percent.

In effect, this was a localized recession — severe in certain places, but concentrated enough that it did not throw the overall United States economy into contraction.

In Williston, N.D., where the economy had been booming for years because of a surge in oil and natural gas drilling on the Bakken oil patch, businesses of all types closed or slashed wages.

 

“It varies week to week, but every week keeps getting worse,” Marcus Jundt, owner of a restaurant, the Williston Brewing Company, told CNBC in March 2016. “We don’t know where the bottom is, but we’re not there yet.”

But it could have been worse.

How it ended

When Janet Yellen assumed leadership of the Federal Reserve in early 2014, she inherited an economy that had been expanding steadily for years, with a great deal of help from the Fed’s interest rate policies.

Deciding how and when to pull that support — when to raise interest rates, which had been near zero for more than six years — was set to be the defining choice of her tenure.

In 2015, with signs that the United States economy was returning to health, she and her colleagues believed it was time to begin raising interest rates. She is a leading labor market scholar who spent a career studying, among other things, how a tight labor market can eventually feed through to inflation.

In July of that year, with stirrings of the emerging markets disruption, the unemployment rate was 5.2 percent, not much above the level Fed officials believed was consistent with a fully healthy labor market. Then the turmoil of August began.

Ms. Yellen elected not to raise rates in September, waiting for more evidence that the economy was truly on track and that the emerging market troubles wouldn’t do too much damage to the domestic economy. But by December she judged that the situation had stabilized enough to raise rates.

At the same time, the Fed revealed forecasts indicating that its senior officials expected to raise interest rates four more times in 2016. Within weeks, global markets were sending a message: Not so fast.

The dollar kept strengthening, the price of commodities kept falling, and the Standard & Poor’s 500 dropped about 9 percent over three weeks in late January and early February. Bond yields plummeted, suggesting that the United States was at risk of recession.

In mid-February 2016, the financial leaders of the world’s most powerful nations were set to convene in a Shanghai for the periodic G20 summit. With global markets in turmoil, the great question was: Can the officials rein in these forces?

The official statement released by the participants in the summit contained multiple nods to the turbulence, acknowledging risks from “**volatile** capital flows” and falling commodity prices. But more important than any words was what followed in the following weeks.

Two days after the summit, China lowered its reserve requirement on banks, essentially opening the spigot for more lending. In the months that followed, it would put in tighter controls on the movement of capital outside the country, and seek to tie the value of the yuan less closely to the dollar.

Three weeks after the summit, the Fed had another policy meeting. Rather than raise interest rates further as had been envisioned in December, Fed officials declined to raise rates — and steeply reduced their expectations of how much further they would raise rates over the remainder of 2016.

Together, these steps were enough to end the vicious cycle. The dollar stopped appreciating and started dropping. **Oil prices** bottomed out and began a recovery. In the United States, capital spending was growing again by the summer of 2016.

What really happened in Shanghai?

Some analysts of **financial markets** have put a conspiratorial bent on the concerted action from the two sides of the Pacific, speculating that leaders had made a secret deal at the G20 meeting in February 2016. They call it the “Shanghai Accord”— essentially, that the Fed would hold off on rate increases if the Chinese also took actions of their own.

Ms. Yellen said it’s not so. She said in an interview that there was an extensive exchange of views and information with the Chinese delegation in Shanghai, but that there were no promises or explicit agreements.

 

“I realize it looked to much of the world like some kind of secret handshake deal,” she said. “This wasn’t a deal. This was the global economy and capital markets affecting the U.S. outlook, and the Fed being sensitive to that, taking that into account and its influencing policy appropriately.”

The Fed, she said, did what it thought was best for the United States economy without knowing exactly what the Chinese would do.

Mr. Sheets, the former Treasury official, also dismissed the idea of some secret agreement.

“It’s just not how it works,” he said. “There were a lot of meetings. A lot of bilaterals and quadrilaterals. You meet with your counterparts and talk about the global economy and think about the challenges and what might be done. But there was nothing agreed behind closed doors that was not part of the formal statement.”

Even if there was no formal secret agreement, the result — leaders of the world’s two biggest economies squarely focused on the risks that the situation presented — turned out to be enough.

The lessons

The impact of the global commodity-currency spiral of 2015-16 is evident from a glance at the economic statistics. It is less so in the economic debates of 2018.

First, while the Trump administration has claimed full credit for a surge in business investment, the bounce-back from the mini-recession is a major factor.

White House economists have presented charts showing a surge starting in the fourth quarter of 2016, when the election took place. But that turnaround began in mid-2016 by most measures, not late 2016 as suggested by the White House’s “six quarter compound annual growth rate” measure.

Second, the mini-recession might well have affected some political attitudes during the 2016 election. While the economy was in pretty good shape for people in large cities on the coasts, 2016 was rough for a lot of people in local economies heavily reliant on drilling, mining, farming or making the machines that support those industries.

A poll in October 2016 by an agriculture trade publication, Agri-Pulse, found that 86 percent of farmers were dissatisfied with the way things were going in the United States.

Third, economic policymakers need to display the flexibility to respond to incoming information, even when it doesn’t fit their own forecasts or preconceptions.

If Ms. Yellen had been more stubborn about sticking to the plan to keep raising rates through 2016 because of her training as a labor market economist, the result might well have been an actual recession. “She’s always learning,” said Julia Coronado, president of MacroPolicy Perspectives, “and not so egotistical that she’s wedded to one view of the world.”

Finally, it shows the global economy is so interconnected that events in Shanghai or São Paulo can cause unpredictable effects in faraway places.

In the last year, the Trump administration has been lobbing tariffs at China and other major economic partners to extract more advantageous terms for trade. But the mini-recession warns of the risk of ricochet.

Like it or not, the complexity of our global connections means that policy can’t just focus on the home front. In 2016, we learned that lesson the hard way, even if not everybody was paying attention.

Pumpjacks and other oil-producing infrastructure outside Watford City, N.D., in 2016. Steady **oil prices** declines caused a collapse in oil and gas investment. | Andrew Cullen/Reuters | If Janet Yellen had been more stubborn about sticking to the plan to keep raising rates through 2016, the result might well have been an actual recession. | Lexey Swall for The New York Times | A news conference before the G20 meeting in Shanghai in 2016. There were rumors of a secret deal. | Aly Song/Reuters

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The New York Times

STOCKS AND BONDS
Business/Financial Desk; SECTB
**An Even Day for Markets Caps a Quarter on the Rise**

By THE ASSOCIATED PRESS
803 words
29 September 2018
The New York Times
NYTF
Late Edition - Final
3
English


American stocks ended back where they started Friday as the **stock market** wrapped up its best quarter in almost five years. Electric carmaker Tesla plunged after federal regulators moved to oust CEO Elon Musk following his tweet last month saying that he was close to a deal to take Tesla private.

Health care companies did better than any part of the market during the third quarter and they continued to rise Friday, while technology companies rose as chip-makers also traded higher. Facebook said it discovered a security breach that affects almost 50 million accounts and its stock fell again, ending its worst quarterly run in six years.

Global banks fell and European stocks skidded after Italy's new government announced a big increase in spending. Italy's main **stock index** fell almost 4 percent as investors worried that the government's plan will lead to a clash with European Union leaders who want Italy to reduce its debt level.

Through the third quarter, pain in other markets led to gains for United States stocks. The Standard & Poor's 500 rose 7.2 percent for the quarter ended Friday, its biggest increase since the end of 2013.

One reason is that investors are worried about other regions, especially emerging markets. The currencies of Turkey and Argentina both dropped during the quarter and investors worried that their currency and economic problems would harm the rest of the world.

''Investors do pivot to the U.S. when they have concerns about other regions,'' said Marina Severinovsky, an investment strategist at Schroders. But emerging markets' stocks have bounced back somewhat over the last two weeks, and Severinovsky said they might do better than American stocks in the fourth quarter.

''The pessimism around those regions is probably too much,'' she said.

The **S**.**&P**. **500 index** inched down 0.02 points on Friday, to 2,913.98. The **Dow Jonesindustrial average** rose 18.38 points, or 0.1 percent, to 26,458.31. The **Nasdaq composite** added 4.38 points, or less than 0.1 percent, to 8,046.35. The Russell 2000 index of smaller-company stocks gained 6.04 points, or 0.4 percent, to 1,696.57.

The spending plans announced by Italy's new government would expand its budget deficit. European Union leaders want Italy to bring down its debt level, which is the highest of any member country after Greece.

Italy's FTSE MIB sank 3.7 percent while the German DAX gave up 1.5 percent. France's CAC 40 lost 0.8 percent and the FTSE 100 index in Britain shed 0.5 percent.

Tesla suffered its worst loss in almost five years. It dropped 13.9 percent to $264.77 after the Securities and Exchange said Musk committed securities fraud with his statement about taking Tesla private.

Facebook fell 2.5 percent to $164.52 after it disclosed the breach. That capped a brutal three months for social media companies. Facebook plunged 19 percent on July 26 after it said user growth had slowed, a drop that slashed Facebook's value by $119 billion, its biggest one-day loss as a public company.

Facebook fell 15 percent in the third quarter and Twitter dropped 35 percent, more than any other **S**.**&P**. **500** stock. Twitter was on a huge run until July 27, when it, too, it reported weak user growth. Investors also worried about the possibility of greater regulation of both companies following hearings in Congress.

"In the U.S. and Europe these companies have largely been allowed, as they've grown to the size and scale and influence that they have, to self-regulate," said Severinovsky, of Schroders. "I think that era is over."

Energy companies rose as benchmark United States crude rose 1.6 percent to $73.25 per barrel in New York. Brent crude, used to price international oils, added 1.2 percent to $82.72 per barrel in London.

Gold rose 0.7 percent to $1,196.20 an ounce. Silver jumped 3 percent to $14.71 an ounce. Copper gained 0.8 percent to $2.81 a pound.

Wholesale gasoline added 0.9 percent to $2.10 a gallon. Heating oil rose 1.2 percent to $2.35 a gallon. Natural gas fell 1.6 percent to $3.01 per 1,000 cubic feet.

**Bond prices** were little changed. The yield on the **10**-**year Treasury** note stayed at 3.05 percent.

The dollar rose to 113.58 yen from 113.42 yen. The euro fell to $1.1610 from $1.1658.

CHART: The **S**. **& P**. **500 Index**: Position of the **S**. **& P**. **500 index** at 1-minute intervals on Friday. (Source: Reuters)

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THE WALL STREET JOURNAL.
U.S. EDITION

**EXCHANGE --- Weekend Investor -- The Intelligent Investor: The 'Dumb' Money Is Bailing on U.S. Stocks --- Individual investors are favoring overseas shares. Sooner or later, they'll look smart.**

By Jason Zweig
916 words
29 September 2018
The Wall Street Journal
J
B5
English


Does it make sense to invest anywhere but in the U.S?

While the **S&P 500** is within 1% of its all-time high, European markets are flat, Chinese stocks are in a deep slump and the Japanese market -- after a huge recent run-up -- has finally clawed its way back to where it was 27 years ago.

Through Aug. 31, the **S&P 500** has outperformed international stocks, as measured by the MSCI World ex USA Index, over the past one, three, five, 10, 15, 20, 25, 30, 35, 40 and 45 years, according to AJO, an institutional investment manager in Philadelphia. Had you put $10,000 in each in 1973 and reinvested all your dividends, your U.S. holdings would be worth $1.06 million; your international stocks, $356,000.

All those numbers seem to indicate you'd be crazy to diversify internationally. But, in fact, all they signify is that numbers can play tricks on you. It still makes sense to add international stocks to a U.S. portfolio, probably more so than ever.

Looking back in time from today, U.S. stocks seem to have dominated over the long run only because they have done so extraordinarily well over the past few years.

Lofted by a strong currency and trillions of dollars of fiscal and monetary stimulus, U.S. stocks rose so swiftly out of the financial crisis that they left the rest of the world behind. That spectacular recovery has obscured the historical record.

The U.S. was among the worst-performing stock markets world-wide in the 1970s and the 2000s; it also earned lower returns than the average international market in the 1980s.

Over the 10 years ended in December 1986, international stocks outperformed the U.S. by an average of 6.2 percentage points annually; even over the decade through December 2007, U.S. stocks lagged the rest of the world by an annualized average of 3.1 percentage points.

No one can say when that might happen again. Chances are it will.

Markets tend to lose their dominance right around the time it seems most irresistible. The Japanese **stock market** rose 22-fold over the 20 years through the end of 1989, making it the world's best major performer.

If you were Japanese, that pinnacle of local outperformance marked the perfect time to diversify outside the country. The Nikkei 225 index, which hit its all-time high of 38915.87 on the last trading day of 1989, remains below 24000 as of this week.

"There have been many historical examples of countries that have risen and then fallen, either their economies or their markets or both," says Marlena Lee, co-head of research at Dimensional Fund Advisors of Austin, Texas, which manages approximately $528 billion.

That's far from saying that the U.S. will become the next Japan. "There's no reason to believe that might happen here," says Ms. Lee, "but you don't have to make that call." If U.S. growth merely slows relative to other economies, stock markets elsewhere in the world are likely to catch up to or surpass the **S&P 500**.

Stocks in the U.S. may be more vulnerable than usual to such a reversal, given how expensive they are. Compared with the rest of the world, U.S. stocks are at their highest valuations on record, according to Bank of America Merrill Lynch -- trading for twice as much, as measured by price to net worth, as international shares.

The rest of the world's markets are less dominated, on average, by technology stocks than the U.S. and more focused on cheaper industrial and financial stocks, says Toby Thompson, a multi-asset portfolio manager at T. Rowe Price Group Inc. in Baltimore, which runs $1.1 trillion. The prices of such stocks outside the U.S. are "a lot more compelling," he says.

What about the common objection that you can globalize your portfolio simply by holding such multinational U.S. companies as Coca-Cola Co. or Intel Corp.?

Because such firms tend to hedge their exposures to foreign currencies, "what the U.S. economy and **stock market** are doing tend to overwhelm whatever benefits the companies get from being global," says Mr. Thompson. Although they are multinational businesses, they still behave like U.S. stocks.

The biggest surprise is that individual investors have not abandoned global diversification during this recent period of disappointment.

Over the past 10 years, even as U.S. stocks hugely outperformed, mutual-fund and exchange-traded-fund investors took $34 billion out of U.S. funds and added $1.02 trillion to international, according to Fran Kinniry, an investment strategist at Vanguard Group.

Historically, investors have chased good returns and run away from bad performance, so "these numbers are kind of crazy," says Mr. Kinniry. "This is incredibly contrarian compared to what we have seen in the past."

Individual investors and their financial advisers, say Mr. Kinniry and other fund executives, seem to be adding money to international stocks as a systematic way of taking some money off the table as U.S. shares keep rising.

Sooner or later, that's likely to make the so-called dumb money look smart.



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**Another Recession Is Looming**

By Martin Feldstein
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28 September 2018
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Ten years after the Great Recession's onset, another long, deep downturn may soon roil the U.S. economy. The high level of asset prices today mirrors the earlier trend in house prices that preceded the 2008 crash; both mispricings reflect long periods of very low real interest rates caused by Federal Reserve policy. Now that interest rates are rising, equity prices will fall, dragging down household wealth, consumer spending and economic activity.

During the five-year period before the last downturn, the Fed had decreased the federal-funds rate to as low as 1%. That drove down mortgage interest rates, causing home prices to rise faster than 10% a year. When the Fed raised rates after 2004, the housing-price bubble burst within two years.

As housing prices plummeted, homeowners with highly leveraged mortgages found themselves owing substantially more than their homes were worth. They defaulted in droves, causing lenders to foreclose on their properties. Sales of the foreclosed properties forced prices even lower, leading the national house-price index to decline 30% in three years.

Banks that held mortgages and mortgage-backed bonds saw their net worths decline sharply. A total of 140 U.S. banks failed in 2009, and those that survived were terrified by how much further the market might slide. To avoid risky bets, they shied away from lending to businesses and home buyers and refused to lend to other banks whose balance sheets were also declining.

The fall in home prices from 2006-09 cut household wealth by $6 trillion. Coinciding with a **stock-market** crash, the erased wealth caused consumer spending to drop sharply, pushing the economy into recession. The collapse of bank lending deepened the decline and slowed the recovery to a sluggish pace.

Fast forward to today. Homes aren't as overvalued as they were in 2006, so there's little chance of an exact replay of the 2008 crisis. The principal risk now is that a **stock-market** slowdown could shrink consumer spending enough to push the economy into recession. Share prices are high today because long-term interest rates are extremely low. Today the interest rate on **10**-**year Treasury** notes is less than 3%, meaning the inflation-adjusted yield on those bonds is close to zero. The hunt for higher yields drives investors toward equities -- driving up share prices in the process.

But long-term rates are beginning to rise and are likely to increase substantially in the near future. Though the 3% yield on 10-year Treasurys is still low, it's still twice as high as it was two years ago. It will be pushed higher as the Fed raises the short-term rate from today's 2% to its projected 3.4% in 2020. Rising inflation will further increase the long-term interest rate as investors demand compensation for their loss of purchasing power. And as annual federal spending deficits explode over the coming decade, it will take ever-higher long-term interest rates to get bond buyers to absorb the debt. It wouldn't be surprising to see the yield on 10-year Treasurys exceed 5%, with the resulting real yield rising from zero today to more than 2%.

As short- and long-term interest rates normalize, equity prices are also likely to return to historic price-to-earnings ratios. If the P/E ratio of the **S&P 500** regresses to its historical average, 40% below today's level, $10 trillion of household wealth would be wiped out. The past relationship between household wealth and consumer spending suggests such a decline would reduce annual spending by about $400 billion, shrinking gross domestic product by 2%. Add in the effects on business investment, and this spending crunch would push the economy into recession.

Most recessions are short and shallow, with an average of less than a year between the start of the downturn and the beginning of the recovery. That's because the Fed usually responds to recessions by cutting the federal-funds rate substantially. But if one hits in the next few years, the Fed will not have enough room to cut rates, as the fed-funds rate is expected to rise to only 3% by 2020. There also won't be much room for a major fiscal intervention. Federal deficits are expected to exceed $1 trillion annually in the coming years, and publicly held federal debt is predicted to rise from 75% of GDP to nearly 100% by the decade's end.

This means a downturn brought on in the next few years by rising long-term interest rates would likely be deeper and longer than your average recession. Unfortunately, there's nothing at this point that the Federal Reserve or any other government actor can do to prevent that from happening.

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Mr. Feldstein, chairman of the Council of Economic Advisers under President Reagan, is a professor at Harvard and a member of the Journal's board of contributors.

(See related letter: "Letters to the Editor: A Looming Recession? Look at Interest Rates" -- WSJ Oct. 4, 2018)

(See related letter: "Letters to the Editor: Feldstein Is More Correct And Subtle on Recession" -- WSJ Oct. 16, 2018)



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THE WALL STREET JOURNAL.

Markets

**Investors Stay Cautious on Banks as Earnings Season Nears; Investor worries about the global economy continue to hang over latest leg of the bull market**

By Amrith Ramkumar
445 words
28 September 2018
05:02 PM
The Wall Street Journal Online
WSJO
English


Bank stocks just suffered their worst week in six months, the latest sign that investors remain cautious on the financial sector even as the U.S. economy grows at the fastest pace in years.

The S&P 500 financials sector fell 4% in the past week, its worst period since March 23, to trim all of its 2018 gains. The decline comes after the group hit a six-month high Sept. 20. The more narrow KBW Bank index of 24 bank stocks has also struggled, lagging behind as the broader stock market has hit fresh records.

The underperformance of financial stocks after the group rose 20% in 2016 and 2017 shows that investor worries about the global economy continue to hang over the latest leg of the bull market, analysts say.

With the Federal Reservesteadily raising short-term interest rates, a flattening yield curve—the gap between yields on short- and long-term Treasurys—is still depressing bank shares. Some analysts expect a flatter curve to continue hurting financials, which borrow money short-term and lend it out at longer maturities, even if the group posts stronger-than-expected earnings when reporting season kicks off in earnest on Oct. 12.

Bank stocks slumped along with the 10-year U.S. Treasuryyield late in Wednesday's session after the Federal Reserve raised interest rates and stuck with projections for more gradual increases ahead. The declines rippled through the broader stock market, pushing the S&P 500 into the red for a fourth straight session of declines.

Some analysts say the sector's recent volatility indicates broader anxiety that a trade war will cut demand for loans, with economic weakness in industries tied to banking, such as the housing and auto markets, continuing to worry investors. Volatility in other growth-sensitive assets like commodities has been another warning sign for money managers.

"It does beg the question: What are they suggesting about where economic fundamentals are heading?" said Jim Paulsen, chief investment strategist at Leuthold Group.

Some investors remain confident in bank stocks, which still ended up 3.9% for the quarter and trade at cheaper levels than the broader market ahead of earnings.

But after the market largely shrugged off the group's steady second-quarter results in July, it's worth keeping an eye on their performance as stocks head into October.

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Write to Amrith Ramkumar at amrith.ramkumar@wsj.com

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THE WALL STREET JOURNAL.

Markets

**Emerging Markets' Double Whammy: Expensive Oil, Weak Currencies; Emerging-market countries and central banks are driven to act as crude climbs to four-year highs**

By Georgi Kantchev and Avantika Chilkoti
993 words
28 September 2018
07:00 AM
The Wall Street Journal Online
WSJO
English


After a turbulent summer, emerging markets face another threat: $80 oil.

Currencies in the developing world have been hit by a toxic mix of global trade tensions, a strong dollar and rising U.S. interest rates. That is making dollar-denominated crude all the more expensive as it climbs to four-year highs.

The price of Brent crude, the international **oil price** gauge, has risen by 22% this year. But the cost has doubled if you're buying in Turkish lira. It is up 39% in Indian rupees and 34% in Indonesian rupiah.

Emerging-market countries and central banks are being forced to act.

India, the world's third-biggest oil importer, is weighing temporarily limiting oil imports, while Brazil and Malaysia have introduced fuel subsidies. On Thursday, central banks in Indonesia and the Philippines raised interest rates to tame rising inflation.

In South Africa, where fuel prices are at a record high, the central bank said in a statement last week that "the impact of elevated **oil prices** and a weaker exchange rate on domestic fuel costs is increasingly evident."

"Emerging markets already have a lot of problems as it is, and when you throw an **oil price** spike to the mix, that creates another big risk factor," said Jon Harrison, managing director for emerging markets strategy at TS Lombard.

The price of oil is rising amid concern about falling supply from Iran, due to U.S. sanctions, and supply outages in Venezuela. Many analysts anticipate even higher prices. Bank of America Merrill Lynch predicted last week that Brent would trade at $95 a barrel by the middle of next year.

Large developing nations like Turkey, India, the Philippines and South Africa import all or most of their oil. So rising prices are spurring higher inflation and expanding already large current-account deficits, a measure of a nation's transactions with the rest of the world. An increasing import bill widens the deficit, which puts further pressure on their currencies.

"Oil is definitely a risk for those pressured by current account funding issues," said Sacha Tihanyi, deputy head of emerging-markets strategy at TD Securities in New York. "If we see oil continuing higher, we'll have to see further monetary and nonmonetary measures in order to help stabilize the external deficit strain."

On Thursday, Bank Indonesia, the country's central bank, raised rates for the fifth time since May. In a statement, the bank pointed to a "surge" in crude imports bringing the country's trade deficit to over $1 billion in August.

Also on Thursday, the Philippine central bank raised its key interest rate, citing rising inflation.

The country's finance minister told Reuters news agency that the recent rise in **oil prices** is his main concern now.

Consumers and companies are feeling the rise in fuel costs.

Last month, India's Jet Airways reported a rise in fuel costs of more than 50% year-over-year in the three months to June. Chief Executive Vinay Dube had already talked of "a tough phase" for the industry, singling out the depreciating rupee and high fuel prices.

Analysts say Indonesian state-owned oil company Pertamina is facing a squeeze as the bill for importing foreign crude soars.

Governments in the developed world, where high **oil prices** can bring street protests and industrial action, face tricky decisions.

Pro-business governments in India and Indonesia face re-election next year. The Indian government had rolled back state subsidies on fuel and introduced fuel consumption taxes as the **oil price** fell in recent years, analysts say. Local media is already lobbying the government to reduce the tax.

The Indonesian government has asked international oil majors in the country, including Exxon Mobil and ConocoPhillips, to sell their local output to Pertamina rather than export it, in an attempt to support the local currency, said Elan Biantoro, a vice president at SKK Migas, the Indonesian oil and gas regulator.

ConocoPhillips declined to comment, and Exxon Mobil didn't respond to a request for comment.

In India, which imports around 80% of its oil, refiners met in Mumbai earlier this month to discuss reducing the country's reliance on imported crude, a spokesperson for Indian Oil Corporation, the country's largest state-owned refiner, said. That could, for instance, include running down inventories rather than buying new oil, he said.

The problem is particularly acute in Turkey, where energy makes up roughly two-thirds of the nation's current account deficit.

Last week, Turkish Finance Minister Berat Albayrak said the only long-term solution was greater energy independence, and he pledged to boost renewable sources of energy.

Still, this isn't the first time that high **oil prices** have coincided with falling currencies and widening trade deficits for emerging markets. In 2013, concern that the U.S. would unwind monetary stimulus sooner than expected prompted selling in emerging market currencies during a period when Brent was trading at over $100 a barrel. Given such experiences, some companies use derivatives to hedge their exposure to currency falls.

"The fact is that we have dealt with higher **oil price** before," says Satrio Tjai, managing director at Rajawali Corp, Indonesia's mining to palm oil group. Mr. Tjai says his company is even benefiting from the rising **oil price**, given a new government mandate that requires diesel fuels to be blended with the biodiesel that Rajawali supplies palm oil to.

Gabriele Steinhauser contributed to this article.

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More on Emerging Markets

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Document WSJO000020180928ee9s001ur

 

WSJ PRO CENTRAL BANKING

Economy

**Consumers Pulled Back Slightly on Spending in August; Strong consumer confidence, rising wages, low inflation and low unemployment should help power spending in the months ahead**

By Harriet Torry
778 words
28 September 2018
01:16 PM
WSJ Pro Central Banking
RSTPROCB
English


U.S. consumer spending cooled slightly in August from the strong pace of growth this spring, although sky-high consumer sentiment bodes well for retailers headed into the holiday season.

Household spending—what Americans paid for all goods and services, such as groceries and health care—rose 0.3% in August from the prior month, the Commerce Department said Friday.

Consumer spending powers the U.S. economy, and August's gain was the smallest since February, marking a modest pullback from a 0.4% increase in both June and July, and 0.5% rises in April and May.

Still, strong consumer confidence, rising wages, low inflation and low unemployment should help power spending in the months ahead.

Consumer sentiment in September was the third-highest level since 2004, according to a University of Michigan survey released Friday. Most of the gain in the final sentiment reading for September was among the bottom third of households by income, whose consumer-sentiment index was the highest since November 2000. A survey by another group, the Conference Board, earlier in the week showed overall household confidence in the U.S. was at its highest level in September since 2000.

The rise in confidence among low-income households was a positive sign for economic growth, since economists have noted that lower-income households have a high propensity to spend additional income.

Friday's report showed Americans are saving less overall. The saving rate in August was 6.6%, the same as in July but down from 7.4% six months ago.

Americans' spending matched the pace of their income gains, which also rose 0.3% in August from the prior month, the government said.

"These data indicate a solid but slowing momentum in consumer spending growth in the third quarter, around 3.5% after a remarkable 3.8% advance in the second quarter," Oxford Economics said in a note to clients.

After the release of Friday's spending and income report, forecasting firm Macroeconomic Advisers estimated gross domestic product expanded at a 3.2% annual pace in the current quarter. The Federal Reserve Bank of Atlanta's GDPNow model predicted a 3.6% growth rate.

The projections for the third-quarter growth rate remain well above the 2% growth seen throughout the expansion. Strong economic growth has also helped power big gains in U.S. stocks in the third quarter, and it has been a key factor in helping investors look past the trade tensions between the U.S. and China and other nations.

"Both household spending and business investment are expanding briskly, and the overall growth outlook remains favorable," Federal Reserve Chairman Jerome Powell said during a press conference Wednesday, after central-bank officials voted to increase their benchmark federal-funds rate by a quarter percentage point to a range between 2% and 2.25%.

Friday's report showed inflationary pressures were modest in August. The price index for personal-consumption expenditures, the Federal Reserve's preferred inflation measure, was flat in August from July, excluding **volatile** food and energy costs. From a year earlier, it increased 2%, hitting the Fed's target for the fourth month in a row.

 

Officials have penciled in one further quarter-point rate increase for 2018. Most Fed officials expect the central bank would need to raise rates at least three more times next year and once more in 2020.

Still, economic growth in the 3% range in the third quarter would mark a slowdown from second-quarter gross domestic product, which rose at a 4.2% seasonally and inflation-adjusted annual rate.

Trade and the impact of recent tariffs are expected to be potential clouds for third-quarter growth. Trade figures released Thursday for August showed the U.S. trade deficit in goods widened for the third month in a row, climbing to $75.8 billion from $72 billion in July.

A widening trade gap, reflecting a decline in exports and a rise in imports, could tug down growth this quarter and mark a reversal from the second quarter, when a narrowing trade gap helped lift the U.S. economy.

The housing market was also a drag on growth for the first half of the year, and the slowdown shows little sign of improving in the third quarter given rising interest rates, low housing inventory and high property prices.

Sarah Chaney contributed to this article.

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THE WALL STREET JOURNAL.

Business

**Former Finance Chief at Salix Settles SEC Charges Over False Statements; Adam Derbyshire allegedly misrepresented drug inventories held by wholesaler customers**

By Micah Maidenberg
637 words
28 September 2018
02:56 PM
The Wall Street Journal Online
WSJO
English


The former finance chief at Salix Pharmaceuticals Ltd. will pay more than $1 million to settle charges that he misrepresented drug inventories held by wholesaler customers several years ago, thereby keeping the company's financial performance and **stock price** artificially elevated.

During quarterly earnings calls with analysts in 2013 and 2014, Salix's then-chief financial officer, Adam Derbyshire, said wholesalers had two to three months of the company's products on hand, when they had significantly more in stock, according to a complaint filed by the Securities and Exchange Commission.

Back then, the SEC alleged, the company was trying to hit revenue targets through "overselling of demand," a practice in which a company creates a bump in revenue by flooding distribution channels using incentives to induce customers to purchase more of its products.

Thomas Sporkin, an attorney at Buckley Sandler who is representing Mr. Derbyshire, said his client had no comment.

Mr. Derbyshire "knew or recklessly disregarded the falsity of his statements," the SEC claimed in the court filing, saying he tracked inventories and was aware wholesalers were resisting Salix's sales efforts "given their already high inventory levels."

Salix is now owned by Bausch Health Cos., formerly known as Valeant Pharmaceuticals International Inc. The SEC's probe predates and is separate from regulators' high-profile investigation of Valeant's former relationship with mail-order pharmacy Philidor Rx Services and other issues. Bausch Health has said it is cooperating with that investigation.

Accounting problems at Salix surfaced in 2014, after a company in talks for a potential takeover of Salix raised questions about the actual level of Salix drugs held by its wholesaler customers. The Wall Street Journal previously reported that Allergan Inc. approached Salix in August 2014 about a takeover but backed away in September that year because of concerns about Salix's inventory levels. After an internal investigation, Salix revealed that wholesaler inventories of two key drugs were much higher than the company had previously signaled, meaning future sales might not have been able to match the level of sales the company had reported in previous quarters.

Salix stock lost more than a third of its value as a result. Valeant purchased Salix in 2015; it subsequently discussed a possible sale of Salix, but no deal was reached.

Salix also settled related SEC charges Friday for its part in Mr. Derbyshire's alleged actions. The company didn't pay a fine but agreed to an injunction forbidding it from future violations of antifraud and corporate reporting provisions of federal securities laws, the agency said.

"The settlement with Salix reflects the company's self-report to the commission and its significant cooperation with the investigation," said David Frohlich, assistant director in the SEC's Enforcement Division. "Salix's proactive remediation included conducting an extensive internal investigation that led to Derbyshire's resignation."

In a statement, Bausch Health said it was pleased to have resolved the situation without a monetary penalty and noted the allegations occurred prior to when Valeant purchased Salix.

"Since the acquisition, Salix has been completely transformed and now operates under the comprehensive compliance programs that govern Bausch Health," the company said.

Mr. Derbyshire's payment includes about $558,000 in disgorgement and interest, plus a penalty of nearly $495,000, according to the SEC. He agreed to be barred for five years from serving as a director or officer at a public company, and also agreed to be suspended from working as an accountant before the SEC.

Both Mr. Derbyshire's and Salix's settlements with the SEC are subject to court approval.

Michael Rapoport contributed to this article.

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THE WALL STREET JOURNAL.
U.S. EDITION

Heard on the Street
**Crypto-Mining IPO Looks as Risky as Crypto Trading**

By Jacky Wong
463 words
28 September 2018
The Wall Street Journal
J
B12
English


[Financial Analysis and Commentary]

Participating in an initial coin offering is pretty risky, but buying into the initial public offering of a leading player in the crypto world could be stomach-churning too.

The world's largest cryptocurrency-mining-equipment maker Bitmain Technologies Ltd. on Wednesday filed for an initial public offering to list in Hong Kong. So far there are no details of how much the China-based company -- which made a $1.4 billion net profit in the 12-month period ended in June -- plans to raise or at what valuation. Almost all of Bitmain's $5.1 billion revenue during the period came from selling mining rigs for cryptocurrencies, mostly bitcoin.

Bitmain will likely find it hard to repeat its stellar year following the boom and bust in cryptocurrencies. Bitcoin, the leading cryptocurrency, has lost two-thirds of its value after hitting a record near $20,000 in December.

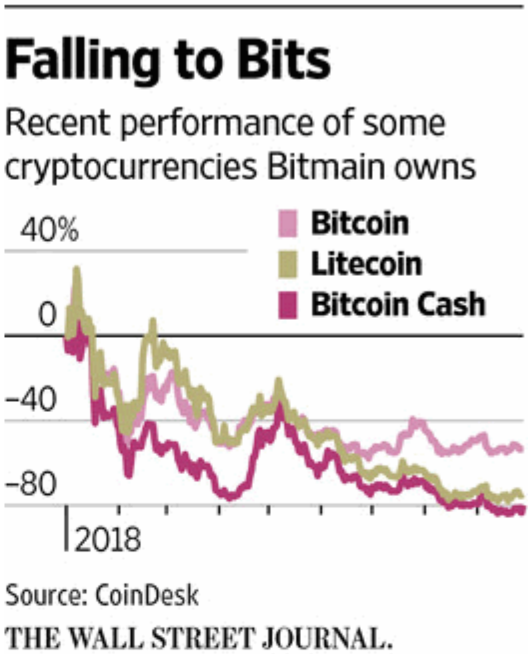
Selling mining rigs -- specially designed machines that can solve the mathematical equations needed to generate new crypto coins -- might look like a more stable business than crypto trading. In reality, Bitmain's business could be just as **volatile**. To start with, the company owned almost $900 million of cryptocurrencies as of June -- more than half of its net assets -- which could lead to substantial losses if the crypto market slides further.

When crypto prices were sky high, Bitmain could sell its rigs at high prices to miners hoping to make a quick buck. But rig prices slumped when cryptocurrency markets went into free fall this year. The average selling price of Bitmain's mining rigs was $1,353 in the second half of 2017, but fell by over one-quarter to $992 in the first half of this year. Current prices are even lower: Bitmain's latest machine that launched last month is selling for $719.

The price slide means Bitmain is likely to prove much less profitable in the current six-month period as its margins narrow. The average cost of manufacturing and materials for each mining rig Bitmain sold in the first half was $576. Costs could fall in the future, but they are unlikely to drop as quickly as selling prices.

The price slide also could lead to further write-downs of Bitmain's $900 million inventory of unsold mining rig equipment. It already logged impairments of almost a third of its stock in the first half of this year. As the arms race in crypto mining rigs heats up, newer machines from rivals are making older models obsolete pretty quickly.

When the gold rushes come to an end, even those selling shovels aren't immune.

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THE WALL STREET JOURNAL.
U.S. EDITION

**Brokers Score Wins On Cost of Data Feeds**

By Dave Michaels and Alexander Osipovich
912 words
28 September 2018
The Wall Street Journal
J
B1
English


Banks and brokerages are starting to win more battles with big **stock-market** operators over the cost of data, threatening a lucrative revenue stream for the New York Stock Exchange and **Nasdaq** Inc.

The Securities and Exchange Commission has recently ratcheted up scrutiny of the **stock-price** feeds sold by exchanges that are used by retail investors, Wall Street banks and high-speed trading firms alike. Several recent SEC decisions represented wins for brokers and traders that have criticized rising data costs.

The five-member SEC also is expected to rule before late October on a major challenge by the brokerage industry stemming from fee increases imposed eight years ago by the NYSE and **Nasdaq** -- a case that could have broader repercussions for the exchanges' data businesses.

Banks and brokerages complain that the NYSE, **Nasdaq** and other exchanges overcharge for data that is essential in today's electronic markets. Exchanges say the fees they charge are appropriate.

"All these fee increases have for years been rubber-stamped by this commission's predecessors," said Douglas Cifu, chief executive of Virtu Financial Inc., an electronic trading firm. "Now you have sensible folks there . . . who are asking the right questions."

In May, the SEC rejected a proposed fee increase for a widely used data feed whose customers include retail brokerages such as TD Ameritrade Holding Corp. as well as search engines such as Google and Yahoo.

The SEC also last week suspended price increases -- which would have become effective without the agency's intervention -- proposed by three options exchanges.

Regulators could still approve the fees, but their move opened an opportunity for critics to tell the SEC why they should be rejected.

The regulator's tougher stance follows a legal reprimand it received last year from the U.S. Court of Appeals for the District of Columbia Circuit.

The appeals court criticized the SEC's approval of a fee plan filed by an options-market clearinghouse, saying the regulator "effectively abdicated" its responsibility to check the merits of the proposal. Exchanges, like the clearinghouse, are self-regulating bodies with latitude to write their own rules, including the fees they charge.

The commission is now poised to weigh in with its biggest decision to date -- a ruling in the brokerage industry's legal challenge, led by the Securities Industry and **Financial Markets** Association. The SEC, which took up the case after one of its in-house judges ruled in favor of the exchanges, plans to announce its decision in October, according to two people familiar with the matter.

Exchanges have emphasized their data businesses in recent years because they provide a predictable revenue stream, unlike trading fees, which vary with volumes.

In addition to offering a basic product that shows current stock prices, exchanges sell more-expensive data feeds that reveal buy and sell orders posted by traders. These richer feeds are mostly targeted at banks and high-frequency traders, who use the information to forecast price changes and pick the best venue for executing a particular trade.

From 2012 to 2017, the combined cost of the richest and fastest equities data from the NYSE, **Nasdaq** and Cboe Global Markets Inc. grew 253%, according to an analysis by R2G, a data-services firm based in Chicago. That amounts to an annual rate of roughly 20%.

R2G estimated the total costs of a broker or high-speed trader buying premium data feeds, including various connection fees.

Intercontinental Exchange Inc. or ICE, the owner of the NYSE, has said sales of real-time **stock-market** data account for about 2% of annual revenue, although that figure doesn't include connection fees paid by large brokers and traders.

"Given their low relative cost within the industry, these real-time products seemingly receive much more publicity and attention than they deserve," ICE Chief Executive Jeffrey Sprecher told analysts on an earnings call last year. **Nasdaq** said in an August report that "the current market for U.S. **stock market** data is efficient and competitive."

ICE and **Nasdaq** declined to comment. Bryan Harkins, executive vice president at Cboe Global Markets, said the company embraces "robust discussions on ways to improve our public markets," including the debate over market data.

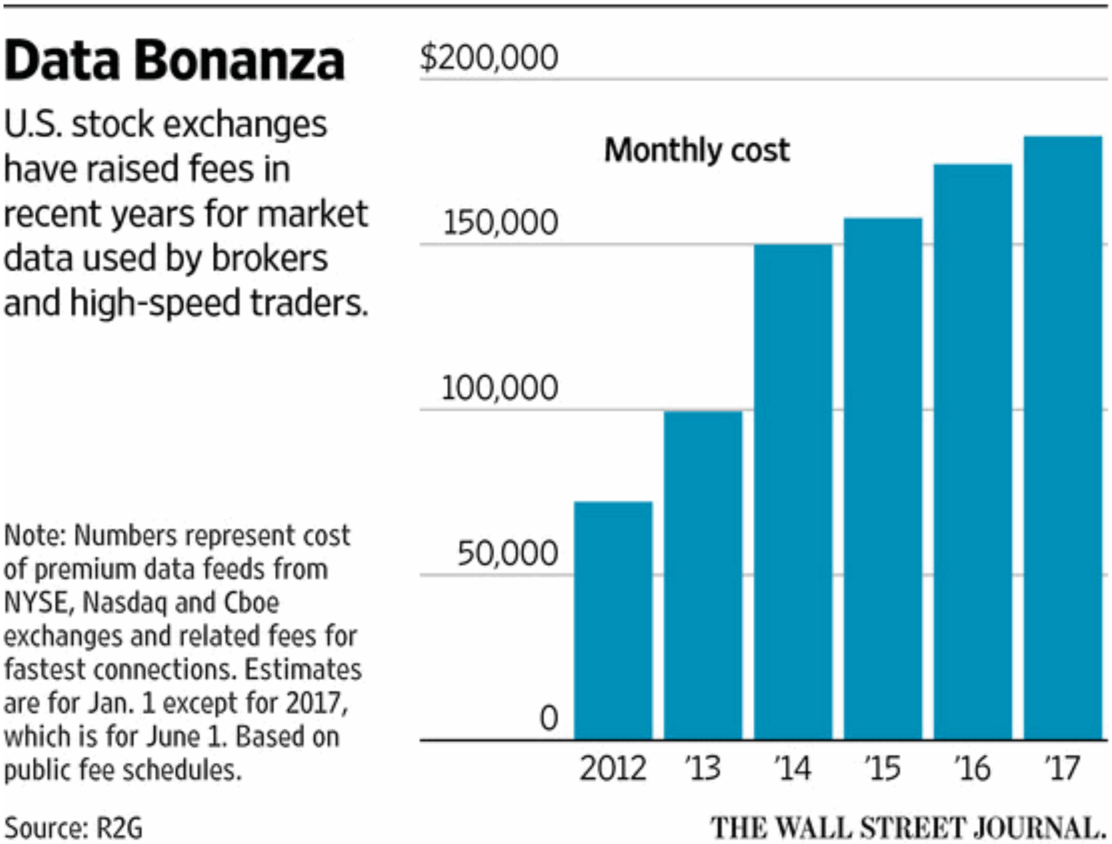
Industry executives credit SEC Chairman Jay Clayton and a new director of trading and markets, Brett Redfearn, for the stepped-up scrutiny of exchange fees. SEC Commissioner Robert Jackson Jr. said last week it was "time for the SEC to get serious about that obligation."

Exchange executives have privately worried that Mr. Redfearn, a former JPMorgan Chase & Co. executive, is biased against them, citing his past criticism of market-data fees. Mr. Redfearn corresponded with Sifma in its legal challenge to the NYSE and **Nasdaq** fee increases, according to court records.

In 2016, while still at JPMorgan, Mr. Redfearn also told an SEC advisory committee that the richest market-data products are "characterized by unconstrained and increasing fees," according to a written statement he submitted for the meeting.

"He has a history around it where he wants to see fees come down," said Mehmet Kinak, global head of systematic trading and market structure at T. Rowe Price Group Inc. "He seems to be somewhat balanced but has a bias like anyone would."

The SEC declined to comment about Mr. Redfearn's past work on the issue. Sifma declined to comment.

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WSJ PRO CENTRAL BANKING

Economy
**BOJ Summary Shows Growing Concerns Over Economy's Downside Risks; Officials at Japan's central bank point to risks posed by international trade frictions**

By Megumi Fujikawa
361 words
28 September 2018
04:58 AM
WSJ Pro Central Banking
RSTPROCB
English


Policy board members of the Bank of Japan are becoming increasingly concerned about downside risks to the economy and prices, including the potential impact of trade frictions, according to a summary of opinions of the bank's recent meeting released on Friday.

"With regard to the risk balance in the global economy, there likely remain growing downside risks stemming from trade friction between such economies as the United States and China as well as from fluctuations in **financial markets**," one of the BOJ's nine policy board members said, according to the summary of the board's meeting held on Sept. 18-19.

Earlier this week, President Trump and Japanese Prime Minister Shinzo Abe agreed to hold talks for a bilateral trade agreement. Mr. Abe appeared to win a promise from President Trump to refrain from imposing auto tariffs on Japan as long as negotiations are ongoing.

The Japanese central bankstood pat on policy at the September meeting after making a number of tweaks in July to prepare for a longer-than-expected fight to lift inflation, which has yet to reach the bank's 2% target. It also reiterated that the bank will allow the 10-year Japanese government **bond yield** to move in a wider range in a bid to revive JGB trading.

One BOJ policy board member said there was more room for the BOJ to consider making its policy more flexible in the future to improve market functions, the summary showed.

A BOJ survey released in early September found sentiment among bond-market participants improved slightly but some analysts said the BOJ's action wasn't enough to prompt further recovery in market sentiment.

The summary of opinions submitted by board members to Gov. Haruhiko Kuroda doesn't identify the members by name. The BOJ releases the summary of opinions in addition to minutes of the meetings as part of its efforts to improve communication with the public.

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THE WALL STREET JOURNAL.

Markets

**Papua New Guinea Breaks Bond-Market Jinx; The Pacific nation of eight million people sold 10-year bonds with a 8.375% coupon**

By Manju Dalal and Julie Wernau
466 words
27 September 2018
03:14 PM
The Wall Street Journal Online
WSJO
English


Papua New Guinea kicked off its first U.S. dollar bond sale Thursday—its fourth attempt since 1999 to sell hard-currency debt, and a test of investor appetite toward the world's riskier borrowers.

The Pacific nation of about eight million people sold bonds offering a 8.375% coupon, lower than the initial guidance, with an order book at roughly $3.8 billion, according to investors, or nearly 20% of the nation's gross domestic product. The timing surprised some investors, coming soon after the collapse of Turkish lira and the Argentine peso, which rattled other developing countries.

However, governments and companies are eager to raise long-term debt before rising global interest rates further increase their borrowing costs. On Wednesday, the Federal Reserve lifted its short-term interest rates by a quarter-percentage point while signaling another increase later this year and more through 2019.

Some investors said the deal was well-timed. Emerging markets equities have erased losses posted over the past month and the JPMorgan Emerging Markets Global Diversified benchmark bond index is up 1% this month.

"People spent all summer selling this stuff," said David Rolley, co-team leader of the global emerging market debt group at Loomis, Sayles & Company. "This feels like a risk plateau."

Targeted Chinese stimulus for infrastructure projects is lifting prices for raw materials and **oil prices** are rising, backstopping emerging market economies that rely on sales of raw materials for growth.

The offering follows extensive roadshows this month where national officials met with investors in Asia, Europe and the U.S. Papua New Guinea had sought to sell five- and 10-year bonds, according to several investors, but later dropped the plan to sell shorter-term debt.

Nate Weisshaar, portfolio manager and senior analyst at Motley Fool Asset Management, said this was actually a "favorable time" to come to market. "Investors are sitting on a lot of money and looking for yields," Mr. Weisshaar said during last week's roadshows.

The deal is large enough to gain entry to a widely tracked JPMorgan bond index.

Papua New Guinea faces numerous challenges, including a shortage of foreign currency and a sharp slowdown in growth in recent years. It is also hosting the Asia-Pacific Economic Cooperation forum later this year, a significant outlay for a small country.

Moody's and S&P Global have said they expect to rate the bonds at B2 and B, respectively, both five notches below investment grade.

Rob Taylor contributed to this article.

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THE WALL STREET JOURNAL.

Markets

**Energy-Company Bonds Surge on Rising Oil Prices; Chesapeake Energy's issue of new bonds on Wednesday were the most actively traded corporate bonds in the U.S.**

By Matt Wirz
409 words
27 September 2018
08:00 AM
The Wall Street Journal Online
WSJO
English


Debt from the energy companies that triggered a junk-bond rout three years ago is surging back on a rally in oil and natural gas prices.

The oil patch accounted for about 29% of all high-yield bonds sold so far this year, and energy sector debt has outperformed debt in other industries.

Case in point, Chesapeake Energy issued $1.25 billion of new bonds on Wednesday to refinance more expensive debt it had borrowed in 2016, and credit ratings firm Moody's Investors Service said it would likely upgrade the company's rating to single-B from triple-C. The new bonds were the most actively traded corporate bonds in the U.S. with $375 million changing hands, according to MarketAxess.

That is a far cry from the existential crisis Chesapeake weathered in late 2015 when stock and bond investors were betting the company would be forced to default.

**Oil prices** are climbing—Brent crude hit an almost four-year high of $82.55 this week—on expectations that coming sanctions on Iran will squeeze supply. Natural gas prices are also on the rise because of low inventory levels.

Those dynamics are likely to keep pushing energy-company bonds higher at least through the end of the year, said Jeffery Elswick, head of fixed income investments at Frost Investment Advisors. Energy companies account for about one-third of the high-yield bonds Frost owns in its flagship $2.9 billion bond fund, up from 10% normally. And energy bonds have risen about 3.25% this year, compared with the 2.5% average for all high-yield bonds, he said. Junk bonds make up about 12% of the fund's total investments.

Companies in the energy and natural-resources industries are capitalizing on investor enthusiasm and have issued $42.5 billion of new high-yield bonds this year, according to data from Dealogic. That is only 2% more than they raised last year, but it compares with a 26% decline in overall junk bond sales over the same period, as rising interest rates—which push **bond prices** down—dampens new issuance in most U.S. corporate bonds.

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THE WALL STREET JOURNAL.

Markets

**U.S. Treasurys Steady After Previous Day's Rally; If U.S. government bonds can't sustain the surge, it could put higher yields in play**

By Sam Goldfarb
738 words
27 September 2018
05:14 PM
The Wall Street Journal Online
WSJO
English


A rally in U.S. government-**bond prices** that followed the Federal Reserve policy meeting stalled Thursday, keeping yields near multiyear highs and suggesting they may have room to climb higher still.

The yield on the benchmark 10-year U.S. Treasury note settled at 3.054% Thursday, compared with 3.059% Wednesday. Yields, which fall when **bond prices** rise, had slid Wednesday after the Fed concluded its two-day meeting.

The Fed raised short-term interest rates, as expected. But its median rate projections for the next two years were unchanged, providing some relief to investors who had been guarding against the possibility of a steeper rate path.

Before Wednesday, selling in Treasurys had pushed the 10-year yield as high as 3.113% on an intraday basis, according to Tradeweb. That was just below its intraday peak this year of 3.119%—a high-water mark dating back to July 2011.

Yields have been rising this month largely because of waning fears about the outlook outside the U.S., as well as continued optimism about the domestic economy. U.S. government-bond yields are closely watched by traders and economists because they serve as benchmarks for a range of interest rates used by consumers, businesses and governments.

While the 10-year yield has climbed more than a half-percentage point this year, it is still low by historical standards. That, and the continued strong demand for riskier debt such as corporate bonds, has ensured that overall credit conditions in the U.S. remain favorable for borrowers.

Fed Chairman Jerome Powell said at press conference Wednesday that the U.S. economy is experiencing a "particularly bright moment," buoyed in part by expansive fiscal policy, higher **oil prices** and strong readings of household and business confidence.

The rally in Treasurys that followed Wednesday's Fed meeting continued into the overnight session, at one point bringing the 10-year yield down to 3.031%, according to Tradeweb.

That yields then reversed course was noteworthy because Treasurys have often sold off heading into major Fed meetings in recent years, only to mount strong rallies afterward. If Treasurys can't sustain a rally this time, it could put higher yields in play; some analysts have suggested the 10-year yield could soon reach 3.25% or even 3.5%.

"The difference now is that the economic data continues to come in pretty strong," said Thomas Simons, senior vice president and money-market economist in the Fixed Income Group at Jefferies LLC. "You look at the tone of Powell's press conference yesterday, he talked a lot more about upside risks than downside risks."

Robust U.S. economic growth is generally bad for Treasurys, because it can encourage the Fed to raise short-term interest rates, cause investors to favor riskier assets and lead to higher inflation, which hurts the value of government bonds by eroding the purchasing power of their fixed returns.

The tax cuts and spending increases that have boosted growth this year have also supported Treasury yields by forcing the federal government to ramp up borrowing, which has led to an increased supply of government debt.

One reason why Treasurys may have steadied after Wednesday's rally is that the Treasury Department on Thursday had to sell $31 billion of seven-year notes, following large auctions of two-year and five-year notes earlier in the week, said Justin Lederer, senior trader of interest rates at Cantor Fitzgerald LP.

"You can't discount the idea that Treasury is raising issuance," Mr. Lederer said. "It can definitely be a factor in the market."

Not all investors are convinced that yields will keep rising. While average hourly earnings climbed 2.9% in August from the year before, there has been no big acceleration in overall inflation.

Yields in other countries also remain extraordinarily low, which has helped to keep a lid on longer-term U.S. yields. The German 10-year bund, for example, yields just 0.53%.

Concerns about the political situation in Italy—along with worries about emerging markets' ability to handle a stronger dollar—have also caused some global investors to shelter in U.S. assets such as longer-term Treasurys.

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THE WALL STREET JOURNAL.

Markets

**Goldman Sachs Enters U.K. Savings Market, Continuing Consumer Push; Consumer bank Marcus provides a way for Goldman to present a friendlier image**

By Margot Patrick
370 words
27 September 2018
07:04 AM
The Wall Street Journal Online
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English


Goldman Sachs Group Inc. entered Britain's £700 billion ($922 billion) cash savings account market Thursday with the U.K. launch of its consumer bank Marcus, adding a fresh source of funding for the U.S. investment bank.

Online-only Marcus offers savings accounts paying interest of 1.5%, the highest rate for instant-access savings products, according to price-comparison websites.

Goldman started Marcus in 2016 in the U.S. as a push into consumer banking, and had said the U.K. would be its second market. The brand has grown rapidly in the U.S., reporting 1.5 million customers, $23.2 billion in deposits and $3.1 billion in loans on June 30.

Starting Marcus has been a way for Goldman to present a friendlier image after gaining a reputation as a villain of the financial world for its involvement in various **financial-market** scandals and sometimes aggressive deal making.

The U.K. website for Marcus, named after Goldman founder Marcus Goldman, shows a child flying a kite in a park and promises in text to put customers at the heart of everything it does.

Shakila Hashmi, head of money at price-comparison site Compare the Market, said Goldman's entry in U.K. retail banking "throws down the gauntlet to the rest of the industry."

She said Marcus's 1.5% interest rate was around three times higher than the average rate on savings accounts from the U.K.'s big banks.

Around 87% of U.K. adults have a cash savings account, according to the country's Financial Conduct Authority. After a 2015 review of the market, it found many consumers were getting a poor deal because they didn't bother switching banks and started making banks give savers more information.

In July, the FCA said those measures hadn't done enough to stimulate competition and that it was considering additional action.

Des McDaid, managing director at Marcus, said "there is a real disillusionment about savings" in the U.K.

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THE WALL STREET JOURNAL.

US

**Buyers See Opportunity as Sales of NYC Luxury Apartments Stay Sluggish; Brokers and analysts attribute the decline to an unsustainable rise in prices earlier, waning urgency and increased inventory**

By Josh Barbanel
964 words
27 September 2018
04:47 PM
The Wall Street Journal Online
WSJO
English


Apartment sales in Manhattan, a bellwether luxury market, continued a long slide during the third quarter, as sales slumped for the third quarter in a row, and inventory of unsold apartments rose.

The third quarter is usually the peak quarter for sales in Manhattan. This year, sales were down 10.3% from the same quarter in 2017. That is the second lowest level for the third quarter since 2011, above the sales in the same quarter in 2016, when sales slowed due to the uncertainty over the presidential elections.

"This is a correction that is needed," said Bess Freedman, co-president of Manhattan-based brokerage Brown Harris Stevens. She said there were many potential buyers who were actively looking at apartments, but holding off waiting for sellers to reduce their expectations and accept lower offers. When prices readjust downward, brokers said, they expected sales to rebound.

Brokers and analysts attributed the decline to an unsustainable rise in prices earlier, waning urgency by investors, and rising supply of both new and resale apartments. Some also cited hesitation by some potential buyers worried about the lingering impact of federal tax changes that reduced the ability of New Yorkers to deduct high state and local taxes, including property taxes.

The slide came despite a **stock market** at or near record highs, which is usually a positive indicator for the Manhattan luxury market, because of the concentration of financial industry jobs in the city.

The biggest decline was logged in sales of condominiums in new buildings, which fell by nearly 37% from the same quarter last year. Brokers said many investors were holding off purchases because a large supply of investor-owned apartments in new buildings had been pushing down potential rental income, especially in luxury buildings.

Sales of older cooperative apartments were also down, by 11.4%, but the median co-op price rose to a record level. Sales of more expensive apartments picked up as sellers lowered prices to make deals. Donna Olshan, who tracks contracts signed on apartments and houses listed for $4 million or more, said the number of contracts signed in the third quarter rebounded by 13% from unusually low levels in the third quarter last year.

Overall the median price of a Manhattan apartment, $1.10 million, was down 4.3% from the third quarter of 2017, while the median co-op price rose by 3.3%, to $855,000. The analysis is based on sales reported to the city as of Sept. 25.

Another sign of the slowdown was a rising inventory of apartments on the market, up 24.1% from the same time last year, according real-estate data site UrbanDigs.com. The absorption rate—the time it would take for a listing to sell at the current pace of sales in September—was 6.2 months, 33% above the rate a year earlier, according to Brown Harris Stevens.

"The third quarter demonstrated beyond any doubt that we have moved into a buyer's market," said Frederick W. Peters, the founder and chief executive of Warburg Realty. He said some buyers were making offers 20% to 25% below asking prices, moves not seen since 2009, in the wake of the financial crisis, when apartment sales plummeted.

He said few sellers were accepting such offers, but they "signal a major shift in our marketplace, one which has been building for at least 18 months."

Pam Liebman, president and CEO of the Corcoran Group, said that buyers have an opportunity to pick up apartments at a discount in a "tough market." "Buyers should be opportunistic now, they have a lot of choices," she said. "The market is suffering from a lack of urgency. The good news is that there are a lot of buyers out there. Traffic has picked up."

Some buyers of Manhattan apartments say they are already taking advantage of the Manhattan market correction. On Wednesday, GAIA Real Estate, a real-estate investment company, paid $52.5 million to buy a batch of 90 condominium units on lower floors at Bridge Tower Place, a 38-story condominium building on East 60th Street near the approach to the Ed Koch Queensboro Bridge from an affiliate of the Brodsky Organization, which built the development in 1999.

Danny Fishman, the managing partner of chief executive of GAIA, said the bulk purchase at below-market prices was based on the expectation that the market correction would continue and apartment prices might drop further before rebounding, after an oversupply of new apartments is absorbed. "We can buy at good prices in good locations with low leverage and wait patiently," he said.

The top sale of the quarter listed in property records was the $74 million sale of three townhouses on East 75th Street near Central Park, that are in the process of being combined.

But the sale might not count in the record books, because the sale wasn't at arm's-length. The sale transferred the title of the properties between Roman Abramovich, a Russian billionaire with ties to the Kremlin who also owns the Chelsea Football Club in London, and his former wife, Dasha Zhukova, a Russian-American art-collector, magazine editor and philanthropist. He paid $88.4 million for the townhouses over several years at a time when townhouse prices were higher.

The next top sale was the $43.5 million sale of a new 7,700-square-foot penthouse with a private rooftop garden, a pool overlooking the Hudson River at 160 Leroy St. in the West Village.

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THE WALL STREET JOURNAL.

U.S. Markets
Markets

**U.S. Stocks Climb, Lifted by Tech Sector; Investors continue to parse the impact of the Fed's rate decision**

By Georgi Kantchev and Jessica Menton
642 words
27 September 2018
05:25 PM
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WSJO
English


U.S. stocks rose broadly Thursday as investors digested the Federal Reserve's decision to raise interest rates and looked ahead to third-quarter earnings season next month.

Eight of 11 sectors in the **S&P 500** climbed as stocks bounced back after turning lower in the final hour of Wednesday's session. Some on Wall Street said the market was shaking off what they thought was a knee-jerk reaction following the Fed meeting.

"You really have to block out the noise in Washington," said Janet Johnston, portfolio manager at TrimTabs Asset Management. "We think the third quarter is going to be stronger than analysts had expected. That's been a pattern that we've seen for a few quarters."

The **S&P 500** rose 8.03 points, or 0.28%, snapping a four-session losing streak, led by the utilities and communications sectors. The **Dow Jones Industrial Average** added 54.65 points, or 0.21%, to 26439.93, while the technology-heavy **Nasdaq Composite** closed up 51.60 points, or 0.65%, to 8041.97.

The **S&P 500**'s new communications sector, which houses Google parent Alphabet, Facebook and Netflix, among other stocks, rose 0.8%, while the technology sector added 0.5%.

Tech-related stocks have helped power much of the gains in U.S. stocks this year, and some portfolio managers expect that to go on.

"Technology is one of the areas that we've seen a lot of growth, and the growth continues," said Ms. Johnston.

Amazon shares rose $38.13, or 1.9%, to $2012.98. Apple climbed 4.53, or 2.1%, to 224.95, boosting the blue-chip index.

Major indexes had pulled back in recent sessions after hitting records late last week. Stocks tumbled Wednesday after the Fed said it would raise short-term interest rates by another quarter percentage point, and central-bank officials signaled they expect to lift them again later this year and through 2019.

A central question for investors is how Fed officials can balance the need to raise rates to keep the economy from overheating without hurting growth in the process. The U.S. economy has been growing at a fast pace this year and the unemployment rate has fallen to multiyear lows.

Companies in the **S&P 500** are expected to report another period of robust profits in the third quarter. FactSet is projecting a 19% increase in earnings, a slight slowdown from the 25% growth posted in the first and second quarters.

"The economic fundamentals continue to be strong," said Guy Miller, chief market strategist at Zurich Insurance Group. But "the pace of U.S. growth will slow with the Fed moves, higher **oil prices** and waning effect of tax cuts."

"This has an impact for the rest of the world, too," he said.

International trade frictions continued to be a focus for money managers after U.S. President Trump accused China of trying to interfere in the forthcoming midterm elections. The two economies have been embroiled in a trade spat this year—both sides have introduced tariffs—and concern is growing about its impact on the global economy. The Trump administration is also stepping up pressure on Canada.

Elsewhere, the 10-year **U**.**S**. **Treasuryyield** fell to 3.054% from 3.059% Wednesday. Yields move inversely to prices.

Overseas, the Stoxx Europe 600 added 0.3%, erasing earlier losses after being dragged down by Italian and Spanish stocks, as investors awaited budget developments in Italy. Asian markets mostly fell, with Japan's Nikkei Stock Average shedding 1%, while Hong Kong's Hang Seng slipped 0.4%.

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THE WALL STREET JOURNAL.

India News
World
**India Raises Some Tariffs to Help Rupee, Curb Deficit; Delhi faces drop in currency, fears impact from U.S.-China trade fight**

By Rajesh Roy and Debiprasad Nayak
383 words
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NEW DELHI—India raised tariffs on some imports in an effort to bolster the weak rupee and tackle its widening current-account deficit.

The rates, which took effect Thursday, have been raised by as much as 10 percentage points on 19 categories of imports which the government considers nonessential, such as air-conditioners, refrigerators, washing machines and jewelry.

The value of India's total imports of products in those categories was 860 billion rupees ($11.84 billion) in the fiscal year ended March, according to a statement by the Ministry of Finance.

The Indian currency has been among the hardest hit as most emerging market currencies fell. The rupee has plunged 14% this year. India's moves come as trade tensions are rising between the U.S. and China as President Trump uses tariffs in his push to shrink America's trade deficits.

Indian officials fear the trade battle could result in some of the Chinese products that were kept from entering the U.S. getting dumped on the Indian market.

Some industry groups welcomed the higher tariffs. "It's a temporary move, but will boost the sentiments for rupee and help contain current-account deficit to some extent," said Ajay Sahai, director general of the Federation of Indian Export Organisations. "In the long-run, these measures could even promote local manufacturing and lead to foreign investments."

Some analysts, however, were skeptical about using higher tariffs to correct trade imbalances. "It may not be a permanent solution to India's current-account deficit woes," said Pranjul Bhandari, chief India economist at HSBC. There is growing evidence that the exporting country's firms adjust the prices downward to retain market shares, limiting the fall in the import bill of the imposing country like India, she said.

India's current-account deficit widened to 1.9% of the gross domestic product in the year ended March 31, up from 0.6% a year earlier.

Market reaction to the higher tariffs was muted. The rupee opened 0.3% higher against the dollar Thursday but later pared its gains as investors returned to worrying about higher **oil prices**.

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THE WALL STREET JOURNAL.

Business

**Petrobras to Pay $853.2 Million to Settle Corruption Probes in U.S., Brazil; Payments stem from involvement in scandal that has rocked Brazilian politics and business**

By Aruna Viswanatha, Jeffrey T. Lewis and Samuel Rubenfeld
882 words
27 September 2018
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English


Brazilian oil company Petrobras has agreed to an $853.2 million settlement with U.S. and Brazilian authorities to end yearslong investigations tied to one of the biggest corruption schemes ever uncovered.

Petróleo Brasileiro SA, as the company is formally known, said Thursday it would pay $682.6 million to a Brazil fund for promoting corporate transparency and compliance and an additional $170.6 million equally split between the U.S. Justice Department and the U.S. Securities and Exchange Commission.

The corruption scandal at the state-controlled oil producer erupted in 2014, when Brazilian prosecutors first announced their investigation into a cartel of construction companies that had been overbilling Petrobras and bribing high-level Brazilian politicians and Petrobras executives along the way.

The investigation, known as Operation Car Wash, has loomed over Petrobras and Brazil ever since. It led to multibillion-dollar losses at the company and slammed its share price, while also sending former Brazilian President Luiz Inácio Lula da Silva and top business executives to jail. The scandal also continues to roil the country's current presidential election campaign.

Several Petrobras executives directly involved in the corruption have been convicted and jailed, including Paulo Roberto Costa, formerly head of the company's downstream division, and Nestor Cervero, former director of international operations. A former Petrobras chief executive, Aldemir Bendine, was also convicted of bribery earlier this year, though on charges related to his time as CEO of state-controlled lender Banco do Brasil.

For Petrobras, the uncertainty over legal repercussions eases considerably with the deal, though analysts caution that there are still lawsuits pending in Brazil and the Netherlands and an arbitration process in Argentina. In the meantime, the company's new management has returned Petrobras to profitability and is working to reduce its mountain of debt, aided by rising **oil prices**.

"It's a new story now. Petrobras is living a new phase," said Raphael Figueiredo, an analyst at Eleven Financial Research in São Paulo, adding that the deal "opens up new opportunities."

Petrobras's preferred shares rose 4.3% to 21.05 reais ($5.26) in Thursday afternoon trading. The share price sank as low as 4.41 reais in 2016, from about three times that just before news of the scandal broke.

The Car Wash probe grew rapidly and ensnared other giant Brazilian businesses, notably construction company Odebrecht SA, which Brazilian prosecutors said was the ringleader in the builders' cartel.

Odebrecht agreed in 2016 to pay $2.6 billion to resolve charges in the U.S., Brazil and Switzerland, with $93 million going to the U.S. The company's former chief executive officer, Marcelo Odebrecht, remains under house arrest after serving 2½ years of a 10-year sentence for corruption charges in a jail cell.

As cast in Thursday's agreement, U.S. prosecutors viewed Petrobras in part as a victim of the conduct of its executives and managers, who were embezzling from the oil company.

The Justice Department agreed not to prosecute the company in exchange for an $85.3 million payment, three years of compliance reports and an admission that the scheme amounted to criminal violations of laws that require public companies to maintain accurate books and records. The company said it will continue to cooperate in ongoing investigations, including of individuals.

One of the laws at issue, the Foreign Corrupt Practices Act, bars U.S.-listed companies—Petrobras is one—from paying bribes to foreign government officials and requires public companies to maintain accurate financial records.

Petrobras admitted that members of its board directed millions of dollars in illicit payments to Brazilian politicians and political parties, prosecutors said. Such payments included bribes directed by one executive to stop a parliamentary inquiry into the company's contracts.

"Executives at the highest levels of Petrobras—including members of its Executive Board and Board of Directors—facilitated the payment of hundreds of millions of dollars in bribes to Brazilian politicians and political parties and then cooked the books to conceal the bribe payments from investors and regulators," the head of the Justice Department's criminal division, Brian Benczkowski, said.

Petrobras reached a related $930 million deal with the SEC, but the agency said it would credit all but an $85 million penalty to a settlement that the company reached earlier this year with investors who had sued the company over the corruption scheme.

The Petrobras settlement, with one-fifth of the penalty amount going to the U.S., is the latest example of U.S. prosecutors working with foreign counterparts to reach a simultaneous agreement with the multinational firm. It also follows recent policy pronouncements by the Justice Department that it wouldn't "pile on" a corporate offender.

Companies and their attorneys have welcomed this approach to corporate criminal settlements, saying it helps them resolve cases that can linger for years and cost hundreds of millions of dollars—even before striking a settlement.

Paulo Trevisani contributed to this article.

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THE WALL STREET JOURNAL.

Opinion

**Another Recession Is Looming; And unlike in the past, the Federal Reserve has little room to encourage growth by reducing rates.**

By Martin Feldstein
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27 September 2018
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English


Ten years after the Great Recession's onset, another long, deep downturn may soon roil the U.S. economy. The high level of asset prices today mirrors the earlier trend in house prices that preceded the 2008 crash; both mispricings reflect long periods of very low real interest rates caused by Federal Reserve policy. Now that interest rates are rising, equity prices will fall, dragging down household wealth, consumer spending and economic activity.

During the five-year period before the last downturn, the Fed had decreased the federal-funds rate to as low as 1%. That drove down mortgage interest rates, causing home prices to rise faster than 10% a year. When the Fed raised rates after 2004, the housing-price bubble burst within two years.

As housing prices plummeted, homeowners with highly leveraged mortgages found themselves owing substantially more than their homes were worth. They defaulted in droves, causing lenders to foreclose on their properties. Sales of the foreclosed properties forced prices even lower, leading the national house-price index to decline 30% in three years.

Banks that held mortgages and mortgage-backed bonds saw their net worths decline sharply. A total of 140 U.S. banks failed in 2009, and those that survived were terrified by how much further the market might slide. To avoid risky bets, they shied away from lending to businesses and home buyers and refused to lend to other banks whose balance sheets were also declining.

The fall in home prices from 2006-09 cut household wealth by $6 trillion. Coinciding with a **stock-market** crash, the erased wealth caused consumer spending to drop sharply, pushing the economy into recession. The collapse of bank lending deepened the decline and slowed the recovery to a sluggish pace.

Fast forward to today. Homes aren't as overvalued as they were in 2006, so there's little chance of an exact replay of the 2008 crisis. The principal risk now is that a **stock-market** slowdown could shrink consumer spending enough to push the economy into recession. Share prices are high today because long-term interest rates are extremely low. Today the interest rate on **10**-**year Treasury** notes is less than 3%, meaning the inflation-adjusted yield on those bonds is close to zero. The hunt for higher yields drives investors toward equities—driving up share prices in the process.

But long-term rates are beginning to rise and are likely to increase substantially in the near future. Though the 3% yield on 10-year Treasurys is still low, it's still twice as high as it was two years ago. It will be pushed higher as the Fed raises the short-term rate from today's 2% to its projected 3.4% in 2020. Rising inflation will further increase the long-term interest rate as investors demand compensation for their loss of purchasing power. And as annual federal spending deficits explode over the coming decade, it will take ever-higher long-term interest rates to get bond buyers to absorb the debt. It wouldn't be surprising to see the yield on 10-year Treasurys exceed 5%, with the resulting real yield rising from zero today to more than 2%.

As short- and long-term interest rates normalize, equity prices are also likely to return to historic price-to-earnings ratios. If the P/E ratio of the **S&P 500** regresses to its historical average, 40% below today's level, $10 trillion of household wealth would be wiped out. The past relationship between household wealth and consumer spending suggests such a decline would reduce annual spending by about $400 billion, shrinking gross domestic product by 2%. Add in the effects on business investment, and this spending crunch would push the economy into recession.

Most recessions are short and shallow, with an average of less than a year between the start of the downturn and the beginning of the recovery. That's because the Fed usually responds to recessions by cutting the federal-funds rate substantially. But if one hits in the next few years, the Fed will not have enough room to cut rates, as the fed-funds rate is expected to rise to only 3% by 2020. There also won't be much room for a major fiscal intervention. Federal deficits are expected to exceed $1 trillion annually in the coming years, and publicly held federal debt is predicted to rise from 75% of GDP to nearly 100% by the decade's end.

This means a downturn brought on in the next few years by rising long-term interest rates would likely be deeper and longer than your average recession. Unfortunately, there's nothing at this point that the Federal Reserve or any other government actor can do to prevent that from happening.

Mr. Feldstein, chairman of the Council of Economic Advisers under President Reagan, is a professor at Harvard and a member of the Journal's board of contributors.

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The New York Times

Business Day; DealBook
**Corporate America and Gender Diversity by the Numbers: DealBook's Closing Bell**

By Stephen Grocer
534 words
27 September 2018
06:05 PM
NYTimes.com Feed
NYTFEED
English


Get the DealBook newsletter to make sense of major business and policy headlines — and the power-brokers who shape them.__________

Corporate America still has a long way to go to improve gender diversity. In March 2017, State Street Global Advisors, one of the largest fund companies, made a push to get companies to put more women on corporate boards. FactSet has now crunched the numbers to see if there has been an improvement since then. The answer: There's a long way to go. The percentage of companies in the Russell 3000 **stock index** with no female board members declined to 18 percent from 23 percent. The percentage of companies in which women hold 15 percent of the board seats or fewer decreased to 47 percent from 58 percent. Currently, the boards of 22 companies have an equal split between men and women, while women make up the board majority at 14 companies, up from five. Just 5 percent of companies in the index are led by women, unchanged from March 2017.

Buybacks may not be such a good thing for investors. A lot has been written about the surge in buybacks this year — they are up 50 percent from a year ago — but a question not often brought up is whether that has been a good thing for investors. Share repurchases have been a go-to move for companies to lift their stock prices over the past decade. But research from TrimTabs Asset Management is raising questions about whether the activity has done much to bolster stock prices. "Many of the companies that have bought their stock back have underperformed the market," wrote Ted Theodore, chief investment officer at TrimTabs, and Vince Chen, a quantitative analyst at the firm. "And that is not just in the recent six months or so — for more than the last three years, an index focused on companies with a strong history of buying back their own stock has underperformed.

President Trump's tariffs are affecting trade, but not in the way he wants. The president has made reducing America's trade deficit a cornerstone of his administration. The White House credited those policies with narrowing the deficit during the second quarter, but that narrative is now unraveling, wrote Ian Shepherdson, chief economist at Pantheon Macroeconomics. The United States' trade deficit in goods widened last month to a six-month high. A slide in exports was the main culprit; they have now declined by more than 1 percent for three straight months. "Now, the data capture the simple point that the U.S. economy's supply-side does not have the slack needed to meet domestic demand pumped up by the tax cuts and government spending increases. The deficit has further to rise," Mr. Shepherdson wrote.

Where are the biggest housing bubbles? UBS has released its Global Real Estate Bubble Index, and the real estate markets in Hong Kong, Munich, Toronto, Amsterdam, London and Vancouver, British Columbia, are all in bubble-risk territory. In the United States, the housing markets in San Francisco, Los Angeles and New York are overvalued.

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THE WALL STREET JOURNAL.

Business

**GenScript Shares Drop on Report Alleging Safety Violations by Unit Partnered With Johnson & Johnson; Research report alleges Nanjing Legend Biotechnology bypassed standard safety procedures while testing experimental gene therapy on Chinese patients**

By Preetika Rana
710 words
27 September 2018
08:36 AM
The Wall Street Journal Online
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English


HONG KONG—GenScript Biotech Corp.'s stock tumbled nearly 27% on Thursday following a research report alleging safety violations by the Chinese company's subsidiary that has partnered with Johnson & Johnson.

The report alleged that Nanjing Legend Biotechnology Co. bypassed standard safety procedures while testing an experimental gene therapy on Chinese cancer patients. It accused parent company GenScript of cherry picking results disclosed to investors. GenScript and Legend deny any wrongdoing.

Little is known about Flaming Research, the compilers of the report. The group's website describes it as a "a team of seasoned equity investors who are sickened by the inability of Hong Kong regulators" to crack down on corporate fraud and who "will be exposing fraudulent companies to protect the interest of minority shareholders."

The website doesn't list a corporate address or a telephone number, and the group couldn't be reached for comment.

Still, the accusations made in its 14-page report spooked investors, forcing GenScript to suspend trading in Hong Kong after its shares slipped to 11.86 Hong Kong dollars.

In December, impressed with early results from patient tests in China, J&J's drug unit paid $350 million for the global rights to co-develop and market Legend's experimental therapy. The companies are testing it on patients in the U.S.

In an email, a spokesman for J&J's drug arm said the company "conducted careful and detailed reviews" of Legend's data and is "optimistic about the potential of this investigative therapy."

Legend's progress is closely watched because it is the first Chinese company to get approval to test a gene therapy in the U.S. It is also one of the few companies testing a CAR-T candidate.

CAR-T therapy involves extracting patients' disease-fighting white blood cells, genetically modifying them to more vigorously attack cancer, then reinjecting them into their bodies. Legend's targets multiple myeloma.

The first CAR-T therapy, Novartis AG's Kymriah to treat aggressive forms of leukemia, was approved last year. The treatment costs hundreds of thousands of dollars for its potential to cure patients.

Among the safety issues at Legend that Flaming Research alleges is an instance where a patient's relative transported cells hundreds of miles from Xi'an, where they were collected at a hospital participating in the gene-therapy research, to Nanjing, where Legend is based and conducts the cell modifications.

Legend Chief Executive Frank Fan told The Wall Street Journal that doctors extracted and sealed the sample, suggesting there was no risk of contamination, and that the relative volunteered to help out because at the time Legend lacked a reliable way to transport samples. Samples are tested for quality before being modified, Dr. Fan said.

China didn't have rules for gene-therapy experiments until a few months ago.

Flaming Research also criticized the company for administering its therapy through regular syringes instead of the intravenous infusions Novartis uses. Dr. Fan said the doses were small enough to be administered through regular syringes and that doing so is safe.

The report said Legend's early results may be flawed because, on follow-up visits, patients were evaluated with blood tests instead of a more accurate bone-marrow biopsy. Dr. Fan said biopsies were done, but not on every visit. The procedure, he said, "is painful and stressful and cannot, and does not, need to be done each time."

GenScript was accused of being selective in what it disclosed to investors, and when, in an attempt to keep its **stock price** high. In one instance, Flaming Research said the company delayed publicly announcing a trial death until after posting promising early results. GenScript said it would respond to that allegation in a statement later.

Even after Thursday's drop, GenScript's share price was three times what it was in June 2017, when Legend unveiled its experimental therapy at a cancer conference in the U.S.

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WSJ PRO CENTRAL BANKING

Economy
**Transcript: Jerome Powell's September Postmeeting Press Conference; Fed chairman discusses the outlook for interest rates, labor-force participation rates and financial stability issues**

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Federal Reserve Chairman Jerome Powell addressed the media Wednesday, Sept. 26, 2018, after the central bank's decision to raise short-term interest rates for the third time this year. He discussed a range of issues, including the outlook for interest rates, strength in the U.S. economy, positive signs in labor-force participation and how financial stability risks appear to be moderate. Here is a transcript of his comments, lightly edited for length and clarity.

JEROME POWELL: Good afternoon, everyone. Thanks for being here. I am going to start with an overview of how my colleagues and I see the economy, what we decided today, and then a bit about our expectations for the months ahead.

Our economy is strong. Growth is running at a healthy clip, unemployment is low, the number of people working is rising steadily, and wages are up. Inflation is low and stable. All of these are very good signs.

Of course, that's not to say that everything's perfect. The benefits of this strong economy have not reached all Americans. Many of our country's economic challenges are beyond the scope of the Fed, but my colleagues and I are doing all we can to keep the economy strong, healthy, and moving forward. That is the best way we can promote an environment in which every American has the opportunity to succeed.

Each time my colleagues and I meet, we face the same question: How can we set policy to best support job growth and low, steady inflation? For many years this question called for very low interest rates to help an economy that had been damaged by the deep financial crisis that gripped the world 10 years ago. As the economy has steadily gained strength, the Fed has been gradually returning interest rates closer to levels that are normal in a healthy economy.

We took another step on that path today with a quarter-point increase in short-term interest rates. These rates remain low, and my colleagues and I believe that this gradual return to normal is helping to sustain this strong economy for the longer-run benefit of all Americans.

As I mentioned, 10 years have now passed since the depths of the financial crisis – a painful part of our history that cost many Americans their jobs, their homes, and for some their hopes and dreams. In addition to holding interest rates low to support the recovery, we have also taken many steps to make the financial system safer. In particular, we're holding the largest banks to much higher standards in the amount of capital and liquidity they hold, and in the ways they assess and manage the risks they take. I'm confident that this system today is stronger and in a far better position to support the financial needs of households and businesses through good times and bad. We continue to work to sustain these fundamental improvements while also ensuring that regulation is both effective and efficient.

Now let me go into more detail about the developments that motivated today's policy decision.

Both household spending and business investment are expanding briskly, and the overall growth outlook remains favorable, and several factors support this assessment. Fiscal policy is boosting the economy. Ongoing job gains are raising incomes and confidence, and overall financial conditions remain accommodative. These conditions are consistent with our summary of economic projections for this meeting. The meeting of committee participants projections for the growth of real [gross domestic product] is 3.1 percent this year and 2.5 percent next year. Job gains averaged 185,000 per month over the last three months – well above the pace needed in the longer run to provide jobs for new entrants to the labor force. The unemployment rate stood at 3.9 percent in August and has been near that level since April.

Smoothing through month-to-month variations, the labor-force participation rate remains about where it was in late 2013 – a positive sign given that the aging of our population is putting downward pressure on participation. We expect the job market to remain strong. And the median of committee participants' projections for the unemployment rate later this year is 3.7 percent, and a bit lower than that in 2019.

Overall, consumer prices, as measured by the price index for personal-consumption expenditures, PCE inflation, increased 2.3 percent over the 12 months ending in July. The core price index – which excludes the prices of energy and food and tends to be a better indicator of future inflation – rose 2 percent over the same period.

The [Fed's rate-setting Federal Open Market Committee] seeks and expects to see inflation remaining near our 2 percent longer-run objective on a sustained basis. At any given time, inflation may be somewhat above or below 2 percent. For example, the recent rise in **oil prices** has pushed inflation a little above 2 percent, but we expect this to be transitory, as is reflected in our projections. The median projections for both the overall and core inflation measures remain very close to 2 percent across the whole projection horizon.

Today, the committee raised the target range for the federal-funds rate by a quarter percentage point, bringing it to 2 to 2¼ percent. This action reflects the strength we see in the economy and is one more step in the process that we began almost three years ago of gradually returning interest rates to more normal levels.

Looking ahead, today's projections show gradual interest-rate increases continuing, roughly, as foreseen in June. The meeting of participants' views on appropriate policy through 2020 are unchanged since the June meeting. These projections play an important role in our work. My colleagues and I believe that it's useful to communicate our views on likely prospects for the economy and for policy.

We are well aware, however, that the economy regularly surprises and that even the most carefully constructed projections are highly uncertain. The projections about the appropriate path of policy assume that the economy evolves, broadly, in line with the projections for growth, employment, unemployment and inflation.

If the economy were instead to falter, lower interest rates would be appropriate. Conversely, if inflationary pressures were to rise more than expected, higher interest rates would be appropriate. Right now, as our statement indicates, risks to the economic outlook appear, roughly, balanced.

Readers of the FOMC statement likely noted that the committee dropped a sentence that indicated that the stance of monetary policy remains accommodative. This change does not signal any change in the likely path of policy. Instead, it is a sign that policy is proceeding in line with our expectations.

We still expect, as our statement says, further gradual increases in the target range for the federal-funds rate, and this expectation is reflected in the projections that I just discussed.

Thanks very much. I'm happy to take your questions.

Q: Thank you. Nick Timiraos of The Wall Street Journal.

Chair Powell, given the lags of monetary policy, I want to know how you think about ending the tightening cycle. How will you know when to stop and do you need to keep going until something in the economy breaks?

MR. POWELL: So the tightening cycle, as you know, is a reflection of the strength of the economy and it's almost three years now that we've been gradually raising rates, and I think the fact that we have moved quite gradually in a way allows us to carefully watch incoming data in the real economy and in the **financial markets** to see how the economy is processing higher interest rates, and the fact that we're moving so gradually I think – I think it limits the long and variable lags problem because, you know, we're being able to raise rates and then wait and see how the economy absorbs these rate increases and, so far, the economy has performed very well and very much in keeping with our expectations.

Q: Thanks. Hi. Jim Puzzanghera from the L.A. Times.

President Trump has stated publicly he's not thrilled with the interest-rate hikes. His comments didn't appear to have any impact on you or your colleagues. Were his comments discussed at your meeting, and do you have any concerns about the effect of these types of comments on the perception of the Fed's independence and your monetary policy?

 

MR. POWELL: So we've been given a really important job to do on behalf of the American people by Congress and we've been given the tools to do it, and my colleagues and I are focused exclusively on carrying out that mission. We consider the best thinking, the best theory, and the best evidence.

We have disparate points of view, which we debate extensively and come to a perspective and try to set monetary policy to achieve maximum employment in a context of price stability. That's what we do. We don't consider political factors or things like that, and so that's who we are, that's what we do, and that's just the way it's always going to be for us.

Q: Steve Liesman, CNBC.

Thank you, Mr. Chairman. Can you explain how – the **stock market** being at or near all-times high, corporate spreads being very tight, how does the level of the market factor into your decisions to raise interest rates? Is there a concern on your part? And then as sort of a second and related part, can you tell us what happens in 2020 and 2021 that – I know you can't tell us – you're shaking your head – (laughter) – that prompts – that prompts you – the Fed to think that rates need to still be above neutral in that time period? Thank you.

MR. POWELL: Sure. So in terms of **financial markets** and monetary policy, we, as we say in our statement every cycle, we do take financial conditions into consideration because broader financial conditions do affect the broader economy and they're one of the many things that we take into account.

The part of it that we control, though, is what we do with the federal-funds rate and that has – that has effects out through, you know, out through the full interest-rate curve and into financial asset prices generally. So the answer is we take – we take everything into account, but, you know, broader financial conditions are just one of the things that we take into account.

In terms of '20 and '21, why – your question was why the funds rate needs to be above neutral. So you're right, some of – some of the participants have mostly very modest overshoots of their personal estimates of neutral a couple or three years out. You know, it's far out into the future. I think it's hard to be confident that that's – that that's the way things are going to be.

What we're going to be doing as we – as we go through time is asking at every meeting whether monetary policy is set to achieve our goals. And I think that that's an assessment of where policy will need to be some years down the road. And I'll leave it at that.

Q: Thanks. Howard Schneider with Reuters.

Chairman Powell, I think – is this too good to be true? Because you've got four years here of unemployment below 4 percent, very low, substantially below NAIRU [non-accelerating inflation rate of unemployment], what appears to be NAIRU, but no reaction of inflation there. And so I don't think that's ever happened since the 1960s. Why do you think it's going to happen now? Or in the alternative, is this forecast for unemployment just being driven by your confidence intervals to the extent that, well, we don't know what else to do so just extend the line out until something happens?

MR. POWELL: No, you're right, the committee forecasts what they – what they show in general is an economy where unemployment remains in the high and middle 3s throughout the entire forecast period and inflation remains very close to 2 percent. That is what the forecast shows. And that is based on our understanding of the way the inflation process works now on the – on the fact that the inflation seems to be fairly nonreactive to changes in slack, that is to say a flat Phillips curve. And it's just – it's a – it's a world of strongly anchored inflation expectations. And that's not just our forecasts, that's many forecasts. So that is – that is – that is the forecast.

So you may ask – I mean, the sense is, what does the longer-run natural rate of unemployment mean? And so that really is a longer-run concept that we think the economy will return to over the longer run. But obviously, that longer run, you know, it's not creating problems in the short run for that forecast.

Now, let's just admit that the inflation process has changed dramatically from where it was in the 1960s to where it is now. It's in a good place now. We can't take for granted that it will remain the way it is. And, you know, we will be, of course, watching carefully if inflation reacts more strongly or more weakly...then we'll adjust policy appropriately.

Q: If I – if I could follow up on that. What are you buying with interest rates –

 

MR. POWELL: Well, interest rates, of course, have effects on growth, have effects – I mean, if – I guess your question was, what are you buying by raising interest rates? The question is, what would the economy look like if you didn't raise rates? It would look very different, I think, if you didn't raise rates.

We're always trying to, you know, work our way between sort of the two – the two problems we face. One is that if we move too quickly, we can, you know, snuff out a recovery unnecessarily and inflation falls short of its 2 percent target. Or if we move too slowly, we have an economy that can overheat. So we're – that's happened through history, we don't see any signs of that now, but we're always trying to navigate between those two shoals and we think that gradually, you know, raising interest rates is the way that we kind of take both of those risks seriously.

Q: Thanks very much. Sam Fleming from the Financial Times.

The Fed has recently been saying that financial stability risks are moderate. What kind of developments could prompt a change in that assessment to elevated risks? And is there an argument for moving the countercyclical capital buffer even when risks are moderate rather than waiting until the risks are seen as elevated, which arguably could be too late? Thanks.

MR. POWELL: So I think one of the most important lessons from the financial crisis is really the importance of the stability of the financial system. And so we – since the financial crisis, as you're aware, we've had a major focus on building up our monitoring of financial conditions and financial stability issues. We've also put in place many, many initiatives to strengthen the financial system through higher capital and better regulation, more transparency, central clearing, margins on uncleared derivatives, all kinds of things like that which are meant to strengthen the financial system. We've done many of those things, and we feel that the financial system's in a much better place.

As we look at – as we look at conditions most recently – and this was at our last meeting and it was in our – in our minutes for the last meeting – quarterly, we have a briefing at the FOMC and also at the board of the staff's views on financial stability, and the staff judged the overall vulnerabilities to be moderate. If you dig into the different aspects of that question, households' balance sheets are in good shape, you know, employment is high, wages are rising, that sort of thing. The banking system, as I mentioned, has, you know, much higher capital, much higher liquidity, is much stronger. If you look at asset prices, it is true that some asset prices are in the upper range of their historical – upper reach of their historical ranges. And then, if you look at nonfinancial corporates, you get – there is the story of leverage there. So it's not that there aren't any vulnerabilities, but we see them as moderate.

Now, you asked about the countercyclical capital buffer. The countercyclical capital buffer is a tool that we added to our tool kit I think, finally, back in 2016. We said that we would deploy it when vulnerabilities were meaningfully above normal. We revisit that on a regular schedule, and the last time we revisited it was, I think, last year – sometime last year, and concluded that the test was not met. As I mentioned at the last briefing, the – you know, the assessment was that vulnerabilities were moderate. But it remains a kit – a tool for our tool kit that we can deploy, you know, when and as we feel appropriate.

Q: Do you see the chances of needing to deploy it as increased?

MR. POWELL: As I said, I think I'm in the camp of seeing vulnerabilities as relatively moderate. I think the financial system – I think another thing that we learned in the crisis is that we need to be alert to the buildup of vulnerabilities as a long expansion continues.

I don't see that in troubling amounts at this point. But, you know, I think it's appropriate for us to monitor that very carefully.

Q: Marty Crutsinger with the Associated Press.

The researchers at the European Central Bank this week put out a paper saying that the impact of a trade war on the U.S. could be dire, that the U.S. economy could drop by 2 percent in the first year after a widespread trade war. Could you talk about the discussion you had? Your policy statement doesn't mention the trade tensions. You did not mention them. Do you – what kind of outlook do you have right now for the trade war?

MR. POWELL: Sure. So I guess I need to start by saying that we're not responsible for trade policy and we don't comment on particular, you know, trade actions and that sort of thing.

But you will have seen that we have this very extensive network of business contacts around the country through the reserve banks largely, and we have been hearing a rising chorus of concerns from businesses all over the country about disruption of supply chains, materials cost increases, and loss of markets, and things like that. So we've been hearing quite a lot of that, and we – the reserve bank presidents talk about it in the meeting and it goes in the minutes. So we – you know, that's – we're very transparent about hearing all of that.

I think if you look at the aggregate – the performance of the U.S. economy at an aggregate, at a national level, it's hard to see much happening at this point. Or you can look at it the other way. You can ask, if all of the tariffs that have been announced are applied, what would be the effect at the aggregate level, and they're still relatively small.

You know, we worry about a couple of things. One is loss of business confidence, which could reduce investment. Again, we don't really see effects that we can measure yet. Also, the possibility of a **financial market** reaction over time to unexpected trade developments.

More than anything, though, I would worry in the longer run where this is going. You know, if the – if the end place we get to is lower tariffs, that would be good. You know, I think trade generally supports productivity, supports higher incomes. And, you know, fair trade – fair trade under internationally accepted rules – can be a good thing. I think if this – perhaps inadvertently – goes to a place where we have widespread tariffs that remain in place for a long time, a more protectionist world, that's going to be bad for the United States economy and for American workers and families, and also for other economies.

Q: Hi. Heather Long from the Washington Post.

This is the third time this year that the FOMC has raised its growth forecast. I'm wondering if you could share a little bit about what's causing that rise and whether you see supply side effects coming through from the fiscal policy, fiscal stimulus yet. Thanks.

MR. POWELL: So it's true. This year has – we've kept raising our forecast for this year. As the year's gone on, the economy has come in stronger than we expected, and that's a really good thing. And the economy, as I mentioned at the beginning, is strong, and there's good reason to expect that to continue.

You ask why. You know, some of it is, no doubt, the effect of the fiscal policy changes, the tax cuts, and the spending increases. That's got to be part of the story. Part of it may be higher **oil prices**, which are calling forth more investment in the oil patch. But, you know, the growth picture is very much supported by very high readings of household confidence, business confidence. So it's a pretty particularly bright moment, I think. If you look back over the last decade, this is a pretty good moment for the U.S. economy.

Q: The supply-side effect?

MR. POWELL: Oh, supply-side effects, yeah. So, you know, we hope they're huge, frankly. You know, the idea is you reduce taxation on corporations and particularly – and allow faster expensing for investment. The idea is to encourage more investment, and that is one of the things that drives productivity, which is one of the main things that drives rising incomes. So the effects are very uncertain. You know, the literature, there's no clear answer to exactly how these mechanisms work or how effective they are. And it would be soon to be seeing supply-side effects. The supply-side effects are probably both more uncertain and they're probably slower to come in. But, you know, as I said, I certainly hope that we'll be marking up our estimates of potential growth as well.

Q: Craig Torres from Bloomberg News.

Taking a page from your risk-management approach in Jackson Hole, Mr. Chairman, I'm wondering if you can talk about what risks would make the committee – plausible risk – go faster in 2019. What risks would make them go slower? If you could talk about scenarios. And then I'd like to ask, do you see yourself as this stimulus tails off, which it does in the forecast, possibly cutting rates to soft land the economy? I know the forecast doesn't show that, but I'm curious how you soft land without doing that.

MR. POWELL: OK. So I think I mentioned in the opening remarks maybe something that addressed your question about what would make us go faster and slower. You know, the main thing where we might need to move along a little bit quicker would be if inflation surprises to the upside. We don't see that. We really don't see that. It's not in our forecast. So I regard that as a risk. I think either significant and lasting correction in **financial markets**, or a slowing down in the economy that's inconsistent with our forecast – those are the kinds of things we'd react to.

In terms of what – you know, what we would do. You know, I think we're always going to be adjusting monetary policy to – in light of conditions on the ground. So if the economy's weakening, then it's very possible we'd be cutting rates and, you know, vice versa. So I can't rule that out. I think it's quite difficult, though, to know what the sort of end effects of fiscal policy are going to be in 2020. It's difficult to know what the policy will be, let alone what the effects will be that far out. So we have to make estimates, but we know that they're highly uncertain.

Q: Hi, Edward Lawrence from Fox Business. Thank you, chairman.

The unemployment rate's now 3.9 percent. The average hourly wages rose 2.9 percent over the past 12 months. Inflation, according to your numbers, holding steady. With the amount of job vacancies that we have out there and the number of people coming back into the workforce this year, where is the point at which we're actually above the natural rate of unemployment and the Federal Reserve should re-examine the consistency of the rate hikes going forward, so not to cool an expanding economy?

MR. POWELL: You mean where is the point at which unemployment is too low?

Q: Right, exactly.

MR. POWELL: Yeah, yeah. You know, so we've been – I think the labor-force participation has surprised us on the upside. There is a long-run trend there and we've now had basically five flat years. If you look – if you look at labor-force participation since the fourth quarter of '13 to now, you really have kind of an oscillation that basically is a sideways movement in the face of a – of a significant downward trend thanks to aging and other factors. That's a gain of well more than a percentage point in participation. So that's really – that's really a good thing. Those are people who are remaining in contact with the labor force and looking for jobs, finding jobs. So that's a great thing.

And it – and it – and it – by the way, it's a signal. It's one of the things that has allowed the unemployment rate not to fall further. And it's a – it's a signal, too, that there may be more there on the supply side, that there may be more labor supply than the prior trend would indicate. So it's a very positive thing to see people staying in the labor force. And, you know, we don't know how long it can continue. We have models and we look at this – we look at this question all the time. And, you know, admittedly, we've been surprised on the – on the positive side here, so we're open to the idea that that may continue or not.

Q: Hi, Jerome. Donna Borak with CNN.

Just to follow up on the tariff question, you said earlier that it seems as the effects of the tariffs so far haven't quite materialized. Those weren't your words verbatim. But Walmart, Gap, Coca-Cola, General Motors, Macy's have all said that they expect the tariffs to affect the prices of everyday consumer goods. So my question is, should there be an effect, when you expect to see that? And at what point do you start to become worried that it's actually going to affect consumer spending and dampening economic growth?

MR. POWELL: It's a concern; it's a risk. You know, so you could see prices moving up. We don't see it yet, but you could see retail prices moving up. The tariffs might provide a basis for companies to raise prices in a world where they've been very reluctant to and unable to raise prices, where raising prices is really difficult, you know, with the ability to shop on the internet. This could provide, you know, a way for – again, we don't see it in the numbers. And, you know, until we see it in the numbers, it's hard to say how one would react.

And the other question would be, if you're just talking about the effect on inflation, is, is it just a one-time increase in the price level or is it actually fueling higher inflation going forward? And that's a real – that's an important question in how we would think about the appropriate response.

Q: But is there a sense of timing in terms of when you might see that kick in, the effect of?

MR. POWELL: I don't see it yet. You know, don't see it yet. But we – you're hearing – I mean, broadly across the economy, it's not just tariffs. You're hearing, we're hearing a lot of talk of labor shortages, of material costs in particular industries. We're hearing, you know, what amount to supply-side constraints and things like that. But we're not seeing it. We're seeing a sort of modest increase in wages, inflation right around 2 percent, no sense of it moving up really, so we're not seeing it yet and, you know, we just aren't. And we're watching very carefully.

Q: Mr. Chairman, Michael McKee, Bloomberg Radio and Television.

Financial conditions are still extremely loose by all the measures that track that. The flow of funds shows a decline in short-term borrowing other than in Treasurys. So I'm wondering if that suggests a change in the way Fed tightening affects the economy. And along those lines, you mentioned that – you dropped the word accommodative doesn't suggest a change in policy. But if you're dropping forward guidance in terms of accommodative, does the dot plot really serve any purpose anymore if, as you say, you can't be confident out to 2021 what's going to happen with the economy?

MR. POWELL: A couple of questions in there. So the dot plot, I mean, it's not new, I don't think it's a new point that forecasts two and three years out – two or three years out are fairly uncertain. The dot plot is individual FOMC participants who are writing down their individual views on the evolution of the economy and of appropriate monetary policy. We don't vote on that, these are individual forecasts. I think market participants generally find that interesting information, so it seems to me to be serving a purpose.

I think the point with accommodative was that its useful life was over. You know, we put that in the statement in 2015 just when we lifted off and the idea was to provide assurance that we weren't trying to slow down the economy, but in fact we were still – interest rates were still going to be pushing to support economic activity. Well, that – you know, that purpose has been well served, and the language now doesn't really say anything that's important to the way the committee is thinking about policy going forward. That's why that came out.

Did I get – did get all of your –

Q: The idea that financial conditions remain loose, even though you've raised rates 200 basis.

MR. POWELL: Yeah. Yeah, you know, it's – if you look at a broad financial conditions index, that's pretty much the answer you'll get. We don't control that. And as I mentioned earlier, we do take financial conditions into account in what we do. And financial conditions are affecting the broader economy, so by definition we're taking them into account.

But if you look at – look at interest rates, you know. Interest rates – look at long-term interest rates this year and short-term interest rates this year, very significant increases. And, you know, with your long and variable lags, that should be – that should be having an effect over time.

Q: Hi. Victoria Guida with Politico.

So Nellie Liang was just put forward by President Donald Trump to the Fed board. And I'm just curious, you know, given that she's a longtime veteran of the Fed, whether you could speak to what role you played in, you know, recommending candidates to the president, giving input on who he should nominate?

And then also, if I – if I may follow up on the financial stability discussion from earlier, you know, you've mentioned before that corporate debt is at high levels. And I was curious whether, you know, you have any qualms about loosening up restrictions on leveraged lending by making that guidance less of a – less of a cudgel, I guess, while – at a time when leveraged lending is gaining steam.

MR. POWELL: OK. So, in terms of nominations to the Fed, those are entirely, completely under the control of the White House and, ultimately, the president. And traditionally, the Fed chair has been consulted on those, and I'm happy to say that that has continued. But these are – these are really decisions for the White House and, you know, we are – think of us as just being consulted.

I will say that I'm very happy and excited about the team that we're putting together, and I'm very much looking forward to having those offices up and down our hall filled. It's been pretty quiet, more – quieter than usual, which is saying something, on the board hall. So we're looking forward to getting some people confirmed.

In terms of corporate debt, so this is a – this is a – you know, I was an investor for a long time, and in areas that were very close to the leveraged lending market. So, you know, I have had a lot of experience in that. That market has evolved really significantly since before the crisis. And, you know, the banks take much less risk than they used to. They're essentially in the – in the business of distributing these loans and bonds rather than keeping them on their balance sheet to a much greater degree.

But it's also true – and there's significant research on this – that excessive risk-taking in the leveraged lending markets does have channels for affecting the real economy if there's overheating and that kind of thing in those markets. So we monitor that carefully.

You know, the guidance isn't binding, as you pointed out. The leveraged lending isn't binding, and that's just the – that's just the way that the law is interpreted.

So it's something we're monitoring. And as I mentioned, we think overall vulnerabilities are moderate.

Q: Binya Appelbaum, the New York Times.

If I can come back to accommodative, do you think of policy as accommodative as present? How close are you to neutrality? And do you share the view of some of your colleagues that you'll eventually need to be restrictive?

 

MR. POWELL: OK. So are we accommodative now? So I think if you look at the – look at the dot plot and the [Fed's summary of economic projections], you'll see that the federal-funds rate even after today's move is below the longer-run neutral estimate of every single participant that – who submits an estimate of that. So that's why this is the perfect time to take the language out, because, you know, it's perfectly clear that there can't be a signal because, you know, by definition that means an accommodative policy. So it wasn't because policy's not accommodative; it is still accommodative. The thinking was more – as I mentioned, it's more that the language has run its useful life.

There's another point, though, too, which is, you know, we don't want to suggest either that we have this precise understanding of where accommodative stops or suggest that that's a really important point in our thinking. You know, what we're going to be doing, assuming we stay on this path, is we're going to be carefully monitoring incoming data from the **financial markets** and from the economy and asking ourselves whether our policy is achieving the goals we want to achieve: you know, sustain the economy, maximum employment, stable prices. That's the way we're thinking about it. That does kind of amount to thinking less about one's precise point estimate of the neutral rate. So that's how I think about that.

Q: Well, the second question is just do you think you're going to end up in a restrictive posture?[Fed] Governor [Lael] Brainard, for example, has said that she expects that you will need to do that. Do you agree with her?

MR. POWELL: It's possible. It's very possible. It happens often and, as I mentioned, many of the participants have written that down and they've written down really modest overshoots, you know, amounting to one rate hike kind of thing, which wouldn't have a big effect on the economy.

You know, I would just say, you know, it really depends on what happens. It depends on if we keep going – you can think of it in different ways. Maybe we've underestimated the neutral rate, maybe we'll be raising our estimate of the neutral rate and we'll just go to that, or maybe we'll keep our neutral rate here and then go one or two rate increases beyond it.

I think it's very possible. But, I mean, ultimately, it isn't really the question we're answering. The question we're answering is how do we provide the economy just the right amount of support – not too much, not too little – to sustain the recovery and achieve our statutory goals.

Q: Thank you, Mr. Chairman. Greg Robb from MarketWatch.

The 10-year anniversary of the bankruptcy of Lehman Brothers got a lot of attention over the last month. I was wondering if you thought there were any lessons from the crisis that you want to share, and two points on that. You go to Congress a lot and talk to members of Congress.

Now, [former Treasury] Secretary [Hank] Paulson and Mr. [Timothy] Geithner [former New York Fed president and former Treasury secretary] and [former Fed] Chair [Ben] Bernanke have said that Congress made a mistake when it took away the Fed's emergency powers in Dodd-Frank. And then one other thing is that are you confident that all these nonbanks didn't – you know, nonbanks never got put into the – you know, the [Financial Stability Oversight Council], you know, system. So are you confident that you can see the risks in the financial system?

Thank you.

MR. POWELL: So three things there. The first thing is the single biggest thing I think that we learned was the – as I mentioned, I think, earlier, the importance of maintaining the stability of the financial system. So I think if you look – if you look back at the way the models worked and the way people thought about risk in the economy, that's what was missing and I think it's not missing anymore. So we – you know, we've put a tremendous focus on that. We raised capital, liquidity. We have stress tests, which force banks to understand – the largest banks, particularly – to understand and better manage their risk and have enough capital to survive a really substantial shock that's at least as bad as the financial crisis. And if all that doesn't work, we've got resolution plans which we've – you know, through many cycles have made really substantial progress, more than I had thought was likely.

So we've done a lot. Nobody's – you know, nobody is, I think, overconfident that we solved every problem and, you know, now we're going back and kind of taking a hard look at everything and, you know, trying to make – trying to keep at it.

So I think those are the really important lessons and, you know, we were determined not to – you know, not to forget them. And that's – I think a risk now is to forget things that we – that we learned – that's just human nature – over time.

 

I saw the article you're talking about. The question is, did Congress take things away – emergency powers from the Fed? So there was sort of a trade for taking away our power under 13 – Section 13(3) to provide support to individual nonbanks, which is really holding companies and other companies. In exchange for that we got orderly liquidation authority and a resolution authority.

Was it a mistake? I don't think there's any sense that Congresses would seriously look at changing that. I have real doubts about whether it was wise to take away our crisis-fighting tools. I think you put them away and you hope you never need them again but – and I certainly strongly oppose efforts to take away more of our tools.

You know, the third thing you mentioned is the designation power so it's a really important power. In my mind, it should be used – my thinking it should be used sparingly and that means, you know, in situations where you have – I mean, in principle you could have another Lehman Brothers come up out of the ground that's not a bank and it could be very threatening or it could be capable of creating systemic risk, and so I think it's a critical power to have. But, again, I would use it – I would tend to use it fairly sparingly.

Q: Nancy Marshall-Genzer with Marketplace.

Are you worried about the effect of rising interest rates on consumers? Credit-card rates have jumped to more than 17 percent since the Fed started raising interest rates. Mortgage rates are up. What do you say to consumers?

MR. POWELL: Yeah. We look – of course, we look at that very carefully. And interest rates are going up across a broad range of consumer borrowing, as they would when we raise short-term interest rates. They're still quite low by historical levels. And the other thing I'll say is take – if you take housing, if you look at the NAR Affordability Index, housing is still more affordable now than it was before the financial crisis.

So you're right that the cost of borrowing is going up, but it's going up from what were extraordinarily low levels. And it is something that we watch carefully. You know, the effect on consumer spending is a very important channel through which interest rates work. And so we do monitor the effects.

Q: Hi. Hannah Lang, American Banker.

[The Office of the Comptroller of the Currency's] decision to go at [Community Reinvestment Act] loans suggests that there's some sort of disagreement among how to proceed with the joint plan. What are the issues that are preventing the joint plan from developing? And how close are you to a possible joint plan?

MR. POWELL: Well, at the Fed we are, you know, deeply committed to the mission of CRA, which is for banks to provide credit and other banking services in the communities they serve. And we have also been of the view for some time that with the evolution of technology, particularly, and changes in the nature of banking, that it's an appropriate time – it's past an appropriate time. It now is certainly an appropriate time to revisit the way we think about CRA.

But we don't want to lose that focus on community. And, you know, we definitely want to see the fundamental purpose of the law sustained.

Many of the issues that we had were reflected in the OCC's [advance notice of proposed rulemaking]. And we're hopeful that over time there will be a joint proposed rulemaking with the OCC, the [Federal Deposit Insurance Corp.] and the Fed. It's a process. And, you know, we're very much interested in continuing to push it forward.

Q: Steve Beckner, freelance journalist, filing for NPR.

Mr. Chairman, following up on the neutral-rate issue – and you touched on this – you and your colleagues slightly lifted the longer-run estimate, the neutral funds rate estimate, to 3 percent. But that's still, I believe, like, 125 basis points below where it was six years ago.

What are the odds that productivity – you know, investment, productivity, labor market, and other developments could further push up the longer-run estimate and possibly make the projected funds-rate levels less restrictive than they now seem?

MR. POWELL: So in principle the historic variables – the long-run growth rate of the economy, the neutral rate of interest, the natural rate of unemployment – don't move quickly. They move very gradually. They're pinned down by longer-run forces like demographics. In the case of the funds rate, it's productivity. It's appetite for safe assets and demographics and other things too. So they move quite slowly through time.

I think we all look at them, those of us who file SEPs every quarter will look at that every quarter and not make a change every quarter, but every now and again make a change. And you're right. We actually – the median ticked up a tenth. It's a tenth we're talking about here.

So but still I think it's a positive thing that people could be raising their estimates of a longer-run neutral rate, and potentially the longer-run growth rate – who knows – and maybe reducing their level of the natural rate of unemployment, which has been the trend. It's just that you change those estimates over time. They're informed by incoming data. They don't change a lot, though, although they did – it's interesting that the neutral rate changed quite sharply after the financial crisis in many different models, and it's been slow to recover. I don't expect a dramatic recovery there.

But, you know, we – we're so bad at forecasting productivity, it's just very hard to know when productivity is going to arrive and in what quantity. So I think we have to be humble about how little we really know about where these starred variables either are or are going.

Q: Hi, Chairman. Paul Kiernan from Dow Jones Newswires. Thank you for taking the question.

I'd like to just kind of ask again – you mentioned earlier that gradual – a gradual pace of rate increases will make it easier to react. But specifically, what are you going to be looking to see? Because you also mentioned, you know, that monetary policy operates with a lag. So any kind of specific signposts that maybe we've reached the end of the tightening cycle or where we should stop?

Secondly, if you worry about the divergence between interest rates in the U.S. and internationally, especially at a time when emerging markets are under pressure. Thanks.

MR. POWELL: Sure. So, you know, some of the things that we'd be looking at to tell us whether we're getting close to supply-side limits would be, first, does job growth slow down? A slowing down in job growth would be an indicator, you know. An unexpectedly sharp increase in wages or inflation could tell you that you're reaching those points. You know, if headline growth slowed down, that's another one. So all of those things would be worth taking into consideration.

I think also, though, we've seen sometimes sharp tightening in financial conditions, as we saw at the beginning of 2016, can have a substantial effect pretty quickly on our economy if it's a broad and significant tightening. So we would be looking for those kinds of things and many other things.

So in terms of divergence, yes, so the U.S. economy is, as I mentioned, is strong and is at a pretty positive moment, you know, with strong growth, healthy labor market, inflation right on target, as I mentioned. And we've seen growth abroad, but growth, I think, both in advanced economies and in some emerging economies has slowed down a little bit. And in that world, you know, if the U.S. is stronger, then that's just part of the context, part of the environment that could mean a higher dollar, it could be – it could therefore mean that some of our demand will wind up being shared with other economies. That's the way the integrated international economy works. So you could see that and, you know, it's just – it's just all of the – all things that go into thinking about, you know, the path of the economy.

I would say, you know, we're not responsible for the dollar. Of course, the Treasury is responsible for managing the dollar. But the dollar has only partly recovered the decline that it had in 2017. It's moved up off its lows, but it's not as high as it was at the beginning of last year yet by a significant margin.

Q: Hi. Jean Yung with Market News International.

Can you give us an update on the technical adjustment in implementing monetary policy that the Fed made earlier this year when it decoupled the interest on excess reserves rate from the upper bound of the target range? And have you been happy with that adjustment? And do you see the need to make another such adjustment in the near future?

MR. POWELL: So we've said that we would use our tools to assure that the federal-funds rate trades within the target range. And the principal tools we use have been interest on excess reserves and then – and then at the bottom end a reverse repo facility. So we – in June when we raised rates, we only raised the interest on excess reserves by 20 basis points and raised the range by 25 and that moved federal-funds sort of back into the range. It worked and it was successful. The federal-funds rate traded in the low 190s, well within the range.

We may – we may do that again. You know, we, again, we have our tools and we will use them. We think it's principally a function just of a number of things, but particularly high Treasurys supply, which is showing up in repo rates and then showing up in fed funds as well. So we don't see it as a – as a – as a big problem. We see it as a problem we can address with our tools and we'll use them if we have to.

Q: Hi, Chairman. Courtenay Brown from Axios.

Last month, the [White House's Council of Economic Advisers] outlined a different way to calculate wage growth. Has the Fed looked at that at all? And what are you seeing in terms of non-wage-based compensation?

MR. POWELL: So I wouldn't comment on a CEA paper. And I would imagine they probably wouldn't comment on our stuff either.

But I would just say this. So I am familiar with the – with the question and the work. You know, we look – we look at a range of indicators of wages and I think the broader the better. You really – a perfect – a perfect wage measure would also include benefits because a lot of compensation these days shows up in the form of benefits rather than wages. So I think it's right to choose those broader ones. But they're kind of all telling the same story right now. If you look at the principal four that we look at, we look at a whole range of wage and benefit cost indicators. They are all now showing wages and benefits around 3 percent growth, right clustered around 3 percent. That's a full percentage point higher than it was five years ago. That's a good thing.

Then the question – the other question is, what about inflation? You know, if you're looking for real wage increases, you've got to ask inflation. And there you have to pick an inflation measure. Some people pick [the consumer-price index]. We, of course, pick personal-consumption expenditures because we think it's a little better measure, it's a little broader. And it tends to run a little bit lower as well, but that's not why we pick it. We just think it's more accurate.

And the trend there is running around 2 percent. So if wages are running at – wages and benefits running at roughly 3 percent and inflation running at around 2 percent, PCE headline inflation is at 2.3 percent, PCE core is at about 2, and I think we see the – you know, the temporary increase in headline inflation as being a function of **oil prices**, probably, and we expect inflation go to back down to 2 percent. So we think of that as 2 percent.

That's how we think about it. I hope that helps.

Q: Myles Udland with Yahoo Finance.

Chair Powell, I want to follow up on something you said, actually, at Jackson Hole. You were talking about longer-term structural challenges for the economy and you mentioned that adjusting the federal budget deficit, which has long been on an unsustainable path becomes increasingly important as a larger share of the population retires. I'm just wondering if you can, you know, maybe expand on your thoughts there, and if this is an issue that comes up among members of the FOMC at all.

MR. POWELL: So it doesn't really come up. It's not really our job. And we do – we do monetary policy. We regulate financial institutions, financial stability, that sort of thing. We don't have responsibility for fiscal policy. But in the longer run, fiscal policy will have a significant effect on the economy. So for that reason, I think my predecessors have commented on fiscal policy, but they've commented on – at a high level rather than trying to get involved in particular – you know, particular measures. And so – and I – my plan is to kind of stick to the same approach and stay in our lane.

And, you know, so I would just say it's no secret it's been true for a long time that with the – with our uniquely expensive health care delivery system and the aging of our population, we've been on an unsustainable fiscal path for a long time. And there's no hiding from it; in the end, we will have to face that. And I think, you know, the sooner the better.

And also, these are good times. These are – you know, this is – this is the economy at nearly full employment or in the range, in the neighborhood of full employment. Interest rates are low. It's a good time to be addressing these things. So I just – I put that out there and leave it at that.

Q: I'm Takesh Khan (ph) with – (inaudible) – newspaper. Thank you for taking my question.

I'd like to ask about emerging market. What do you think about impact of U.S. monetary policy on emerging market, especially currency depression or capital – the flow from the emerging countries?

And do you think there is a possibility to stop the interest-rate hike due to emerging market turmoil – due to turmoil of emerging market?

 

MR. POWELL: Sorry, the second question was?

Q: There is a possibly to stop the interest-rate hike.

MR. POWELL: Oh, to stop, OK. All right.

Well, we serve a domestic mandate which is assigned to us by Congress, and that is to have maximum employment and stable prices...[and] the performance of the emerging market economies, really, really matters to us in carrying out our domestic mandate.

I'd also say that, you know, a strong U.S. economy where Americans are buying things and the economy is growing and our – you know, that's going to support demand all around the globe. So that's a good thing.

Now, we do understand, though, that when we – when our economy is strong and we're raising rates, that puts upward pressure on interest rates around the world and can affect countries, particularly countries that have significant external dollar borrowing. And what we try to do is be very transparent about what we're doing and why, and we have been I believe, and we've also moved quite gradually. So I – you know, I think we've been performing well on that front.

There are some countries that are – that are undergoing severe stress, a handful of them, and – but not most emerging market countries. It's a relatively small number. And those particular countries have – you know, have particular vulnerabilities which are well known in the form of budget deficits and significant external dollar borrowings and high inflation and things like that.

So, again, well continue to conduct U.S. monetary policy as transparently as we possibly can. And that's really the best thing we can do, along with supporting U.S. growth.

I'll just – I think that answers both your questions, actually.

Q: Jeannie Monte (sp) with Agence France-Presse.

You mentioned earlier a possible, not probable, correction. And I want to come back to the high level of the **stock market**. Are there any participants to the FOMC who think that we are witnessing an episode of irrational exuberance or rational exuberance? And if there was a steep correction, would it provoke financial stability concerns?

MR. POWELL: So I don't comment on the appropriateness of the level of stock prices. I can say that, by some valuation measures, they're in the upper range of their historical value ranges. But, you know, I wouldn't want to – I wouldn't want to speculate about what the consequences of a market correction should be.

You know, we would look very carefully at the nature of it. And, I mean, really what hurts is if consumers are borrowing heavily and doing so against, for example, an asset that can fall in value. So that's a really serious matter when you have a housing bubble and highly levered consumers and housing values falling. We know that that's a really bad situation.

A simple drop in equity prices is – all by itself doesn't really have those features. It could certainly feature – it could certainly affect consumption and have a negative effect on the economy, though.

Q: Thank you, Mr. Chairman. Mark Hamrick with BankRate.com.

One thing that's changed since the crisis is the majority of mortgages issued last year came from so-called nonbank lenders, as traditional banks scaled back. What confidence do you have about supervision, and I suppose also regulation in this space, given the role of housing finance in the crisis? Thank you.

MR. POWELL: It's a good question. So you're right that a lot of mortgages now originate outside the system. Many of those, though, have to meet certain basic standards to be bought by the [government-sponsored enterprises]. I think we – if we look at mortgage credit more broadly, though, what we see is that credit is pretty widely available to people with high scores and with good credit, good credit records, and much, much less available than it was before the crisis to people with low scores and perhaps troubled credit history.

You know, it's – have we set – have we got that exactly right? I don't know. I mean, I – but that's clearly – that's the reality.

 

In terms of those institutions, they do have supervision by the [Consumer Financial Protection Bureau] and other state regulators. But you're right. They're – much of the origination process has moved outside the banking system. It's something we monitor.

More

* Fed Raises Interest Rates, Signals One More Increase This Year

* The Fed Isn't the Supreme Court. Thank Goodness

* Heard on the Street: Accommodative or Not, Rates Are Going Up

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WSJ PRO CENTRAL BANKING

Economy

**The Fed Isn't the Supreme Court. Thank Goodness; In a charged partisan environment in Washington, the central bank remains for now an apolitical island**

By Greg Ip
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While many Americans are riveted on the Supreme Court this week, they might have missed an action by another federal institution that will affect almost every household.

That the Federal Reserve's interest rate increase drew relatively little attention is a good thing. As American institutions from the courts to law enforcement have become partisan battlegrounds, the central bank for now is an island of dull, apolitical competence.

A few years ago, this didn't seem likely. The Fed emerged from the financial crisis under attack from the left for bailing out bankers and from the right for unconventional policies to hold down interest rates and stimulate spending.

As a candidate, Donald Trump joined in with his own attacks. As president, he had an unprecedented opportunity to appoint bomb throwers or partisan loyalists to the top positions at the central bank, including chairman and vice chairman.

He didn't.

He has nominated mainstream, qualified candidates who have mostly drawn praise from outside economists and Fed watchers. It isn't a guarantee the Fed won't err—by raising interest rates too slowly or too quickly—but it provides essential stability to the economy's most important institution.

It helped that the partisan activists who care deeply about the judiciary, law enforcement, the environment and immigration were less invested in the Fed.

Some Republican legislators did believe former Chairwoman Janet Yellen and her predecessors had kept interest rates too low and lobbied for John Taylor, a Stanford University economist, to succeed her. But Mr. Trump actually liked Ms. Yellen; he just wanted her policies carried out by his own appointee.

Stephen Moore, a scholar at the Heritage Foundation who advised the president to select Mr. Taylor, says, "Trump was worried that Taylor would be too hawkish on inflation."

Instead, Mr. Trump nominated Jerome Powell, a Republican previously appointed to the Fed by Barack Obama and championed by Treasury Secretary Steven Mnuchin.

Mr. Trump seems surprised Mr. Powell has continued raising interest rates. "I'm worried about the fact that they seem to like rising interest rates," he said Wednesday. "We can do other things with the money."

Despite his public grumbling, Mr. Trump hasn't pressured Mr. Powell by nominating loyalists to vacancies on the Fed's board of governors.

The search process for Fed candidates began soon after Mr. Trump took office and was coordinated by Andrew Olmem, a former Capitol Hill staffer who is now deputy director of the National Economic Council.

The result has been a slate of governors with complementary backgrounds in monetary policy, bank regulation, management and **financial market** stability. Three—Richard Clarida, a monetary economist; Randal Quarles, a banking lawyer; and Michelle Bowman, Kansas' banking commissioner—are Republicans. Nonetheless, all were backed by some Democratic senators.

Last week Mr. Trump nominated Nellie Liang, a former Fed staffer specializing in financial stability, for the board's last vacancy. Some Republicans wonder if Ms. Liang, a registered Democrat, may be too fond of regulation. But she has drawn praise from conservatives, such as at the Manhattan Institute, a think tank.

It is too soon to judge the impact of Mr. Trump's appointees. And controversy is inevitable, over both interest rates and regulation. Democrats criticized the Fed's decision to offer Goldman Sachs and Morgan Stanley a pass on recent "stress tests" (though Lael Brainard, the only remaining Obama appointee on the board, backed the move.) But the Fed has moved more gradually to ease rules than Trump appointees at some other financial regulators.

Fed officials have also been helped by the central bank's deeply ingrained tradition of nonpartisanship. Republican legislators often criticized Ms. Yellen and her predecessor Ben Bernanke; they didn't fire back, but nor did they change course. Mr. Powell has done the same, refusing to wade into charged topics such as tariffs and tax cuts except insofar as they affect the Fed's job.

The Fed's culture has a way of absorbing newcomers. While federal judges bring their own clerks and cabinet secretaries their undersecretaries, Fed chiefs come alone. Their advisers and secretaries are drawn from the existing central bank staff, which reinforces continuity (and group think, say critics).

Mr. Powell has recruited Johns Hopkins University academic Jon Faust as an adviser, but they got to know each other when Mr. Faust served on the Fed staff. That staff is itself relatively diverse ideologically; Ms. Yellen, once chairwoman of President Bill Clinton's Council of Economic Advisers, was once a staffer, as was Kevin Hassett, now chairman of Mr. Trump's CEA.

In its approach to policy, however, the Fed is rather homogenous. "We consider the best thinking, the best theory, and the best evidence," Mr. Powell said Wednesday. "We don't consider political factors or things like that, and so that's who we are, that's what we do, and that's just the way it's always going to be for us."

Write to Greg Ip at greg.ip@wsj.com

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**Fed Raises Rates; Indonesia, Philippines Follow; Suit Could Complicate Fed Rate Policy; The Wall Street Journal's central banking newsletter for Wednesday, September 27, 2018**

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The ‘Dot Plot' Reveals Two Policy Directions

By Nick Timiraos

It's generally a mistake to obsess over the interest-rate projections—the so-called dot plot—in the out-years of the Federal Reserve's quarterly economic projections. Nevertheless, the projections released Wednesday highlight two different directions policy could move after next year.

Most Fed officials see the central bank raising rates by another percentage point through next year. The question then turns on what happens after that, when rates will be well within the range officials currently estimate is likely to prevail over the long run.

Looking ahead to 2020, the median projection shows just one more rate increase, to a range between 3.25% and 3.5%.

Look closer, and there are only two officials who project such a level of interest rates. Rather, there's a cluster of seven officials who expect the Fed will need to raise rates above 3.5% and another cluster that says rates shouldn't need to rise beyond 3.25%.

The split likely reflects different opinions over how inflation is likely to behave. Wednesday's projections show all officials see inflation holding between 2% and 2.3% over the next three years. The dot plot shows, however, that officials expect a different rate will be needed to keep inflation at that range.

The strength of the Phillips curve could largely determine which of the two camps prevails. The first camp says so long as unemployment keeps falling farther below the level they project is consistent with low and stable inflation, the Fed will need to raise rates to prevent the economy from overheating. This is an uncontroversial strategy because it is what the central bank always does at this point in an expansion.

Another camp argues for a relatively radical departure from this norm. These officials say if inflation doesn't appear to be accelerating beyond 2%, the Fed could stop raising rates after reaching a neutral setting that neither spurs nor slows growth, even if unemployment remains at very low levels.

Mr. Powell didn't say where he stood on Wednesday, but he continued to voice some uncertainty over the traditional models that have animated the Fed's thinking. "Let's just admit that the inflation process has changed, dramatically, from where it was in the 1960s to where it is now. It's in a good place now," he said.

Officials will be "watching carefully," he said. "If inflation reacts more strongly, or more weakly, to the strong economy, then we'll adjust policy appropriately."

Fed Raises Interest Rates, Signals One More Increase This Year

The Federal Reserve said it would raise short-term interest rates by another quarter-percentage point, and officials signaled they expected to lift them again later this year and through 2019 to keep a strong economy on an even keel. Officials voted unanimously Wednesday on the increase, which will bring the benchmark federal-funds rate to a range between 2% and 2.25%. Most Fed officials expected to raise rates one more time this year, according to new projections released after the meeting. "Our economy is strong," Fed Chairman Jerome Powell said in a news conference.

How the September Statement Changed From August

Analysis: Powell Says It Was Perfect Time to Strike 'Accommodative'

Heard on the Street: Accommodative or Not, Rates Are Going Up

Bank Suit Could Complicate the Fed's Rate Policy

A lawsuit against the New York Fedcould complicate the central bank's effort to control short-term interest rates at a time when investor scrutiny of those markets is intensifying. TNB USA Inc. contends in a federal suit filed in late August that it has been wrongly blocked in its pursuit of a "master account" at the Fed that would allow it to earn interest on deposits placed on the Fed's books.

Mexico's President-Elect to Nominate Economist to Central Bank

Mexican President-elect Andrés Manuel López Obrador intends to nominate well-known independent economist Jonathan Heath to the Bank of Mexico's board of governors in his first central bank appointment, according to people with knowledge of the plan.

Czech Central Bank Raises Rates Again

The Czech National Bankraised its key interest rate for the sixth time in just over a year, cementing its position as the most dynamic of Europe's central banks in charting a path back toward policy settings that were considered normal before the global financial crisis.

Bank Indonesia Hikes for Fifth Time Since May

Bank Indonesiaraised interest rates for the fifth time since May, and said it would introduce trade in domestic non-deliverable forwards for the rupiah to reduce exchange-rate **volatility**. The central bank raised the benchmark seven-day reverse repo rate by a quarter of a percentage point to 5.75%.

New Zealand Central Bank Keeps Rates On Ice

New Zealand's central bankleft its benchmark interest rate unchanged while continuing to leave its options open for the future, saying the next move could be up or down. The Reserve Bank of New Zealand held its benchmark official cash rate at 1.75% as expected by economists, a level it has been maintained at for nearly two years.

Philippines Central Bank Raises Interest Rates

The Philippine central bankraised overnight interest rates, as expected, citing rising inflation. The central bank's benchmark lending rate was raised to 5.0% from 4.5%, while the borrowing rate is now at 4.5% from 4.0%. All 11 economists polled by The Wall Street Journal had expected a rate increase.

FINANCIAL REGULATION ROUNDUP

SEC Tech Chief Heads to Federal Reserve Bank of New York

The U.S. Securities and Exchange Commission's chief information officer is heading to the New York Fed, to serve as CIO and executive vice president of technology, the agency said. Pamela Dyson has served as the financial regulator's top information-technology official for the past three years,

Regulators Raked in $26 Billion in Global Penalties Since 2008

Sanctions violations accounted for 56% of all fines handed out by regulators around the world in the past 10 years, a new study shows. The U.S. is by far the most financially punitive regulator, according to compliance services provider Fenergo. The U.S. accounted for 91% in value of the $26 billion in penalties levied since 2008 for anti-money-laundering, sanctions and know-your-customer breaches, the firm found.

Foreign Real-Estate Buyers Get Told to Go Home

From increasing taxes to zoning to barring access to credit, nations on every continent in the world are using a range of creative barriers to restrict foreign home buyers. Here are some of the most recent efforts across the globe.

Thursday

 

8:30 a.m. EDT

U.S. Commerce Department releases August durable-goods data

U.S. Commerce Department releases third estimate of second-quarter GDP

9:30 a.m. EDT

ECB's Draghi speaks at European Systemic Risk Board conference in Frankfurt

10 a.m. EDT

Bank of England's Carney, ECB's Villeroy de Galhau and Riksbank's Ingves speak on panel at European Systemic Risk Board conference in Frankfurt

11:30 a.m. EDT

ECB's Lane speaks at European Systemic Risk Board conference in Frankfurt

1 p.m. EDT

ECB's Praet speaks in London

2 p.m. EDT

Dallas Fed's Kaplan speaks at forum for minorities in banking in Charlotte, N.C.

4:30 p.m. EDT

Fed's Powell speaks on U.S. economy in Washington

6 p.m. EDT

Bank of Canada's Poloz speaks in Moncton, New Brunswick

7:50 p.m. EDT

Bank of Japan releases summary of opinions for Sept. 18-19 meeting

Friday

8:30 a.m. EDT

U.S. Commerce Department releases August personal income and outlays

8:35 a.m. EDT

ECB's Praet speaks on panel at European Systemic Risk Board conference in Frankfurt

9:20 a.m. EDT

Bank of England's Ramsden speaks in London

10 a.m. EDT

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

4:45 p.m. EDT

New York Fed's Williams speaks at Columbia University in New York

How the Fed Can Help Working Women

Tame inflation and restrained wage growth aren't the only reasons why the Fed should take it easy on rate increases, Karl W. Smith writes for Bloomberg Opinion. "Historically, tight labor markets have tended to empower the less privileged, particularly women and minorities. The Fed should be careful not to undercut this trend before it has a chance to affect women throughout the job market." He adds that "an improvement in women's employment status has corresponded with an increased willingness of women to challenge abuses in the workplace. The social dynamics underlying this movement are of course complex. But if one of the factors preventing women from speaking out was fear of losing their job or damaging their career, then a robust labor market can help. It cannot remove these threats, but it can soften them."

Fed Raises Interest Rates, Signals One More Increase This Year

Sales of new homes in the U.S. rebounded in August, following two months of declines.

Large corporations like Amazon.com demand low prices from suppliers. That holds down consumer costs, but may also crimp worker pay.

The International Monetary Fundagreed to boost its bailout package signed with Argentina in June. The new agreement will increase the bailout size by almost 15% to $57.1 billion.

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

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Document RSTPROCB20180927ee9r000m9

WSJ PRO CENTRAL BANKING

Economy

**Aircraft Demand Propels Increase in U.S. Durable-Goods Orders; The rise was the best gain since February and well above economists' estimates**

By Eric Morath and Sarah Chaney
358 words
27 September 2018
08:35 AM
WSJ Pro Central Banking
RSTPROCB
English


WASHINGTON—Demand for long-lasting goods produced by U.S. factories took off in August due to an increase in aircraft orders, but an underlying measure of business investment fell.

Orders for durable goods, reflecting manufactured products intended to last at least three years, rose a seasonally adjusted 4.5% in August from the prior month, the Commerce Department said Thursday.

It was the best gain since February and well above the 2.1% improvement economists surveyed by The Wall Street Journal had expected.

August's advance largely reflected a 69.1% increase in orders for civilian aircraft, a highly **volatile** category. Meanwhile, orders for automobiles and parts fell 1% on the month.

When excluding transportation orders, demand rose 0.1% in August.

Through the first eight months of 2018, overall orders are up 9.2% versus the same period the prior year. Excluding transportation, orders through August are up 8.2%. Both figures are consistent with broader strengthening for U.S. manufacturers who are finding solid business and consumer demand for their goods.

A closely watched proxy for business investment, orders for nondefense capital goods excluding aircraft, fell 0.5% from July. The category had increased the prior two months. Through the first eight months of the year, those core orders are up 7.4% from the same period in 2017.

The tax overhaul President Trump signed into law last year was designed to incentivize businesses to step up investment. Increased orders this for items such as machinery and metals may reflect the law is working as intended, though other factors are also at play. One is **oil prices** moving this year to the highest levels since 2014, sparking investment in the domestic energy industry.

Orders for defense goods, another **volatile** category, rose 44.4% in August from July. Excluding defense orders rose 2.6% on the month.

Write to Eric Morath at eric.morath@wsj.com and Sarah Chaney at sarah.chaney@wsj.com

Document RSTPROCB20180927ee9r000b5

THE WALL STREET JOURNAL.
U.S. EDITION

**Fed Increases Interest Rates, Signals One More Bump in '18**

By Nick Timiraos
893 words
27 September 2018
The Wall Street Journal
J
A1
English


The Federal Reserve said it would raise short-term interest rates by another quarter-percentage point, and central-bank officials signaled they expected to lift them again later this year and through 2019 to keep a strong economy on an even keel.

The policy makers voted unanimously Wednesday to lift their benchmark federal-funds rate to a range between 2% and 2.25%. Most Fed officials expected to raise rates one more time this year, according to new projections released after the conclusion of their two-day rate-setting meeting.

The increase, which drew a rebuke from President Trump, is the third this year and the eighth since the Fed began to lift rates in late 2015 after keeping them pinned close to zero after the 2008 financial crisis. The Fed's action marks the first time it has lifted its benchmark rate above 2% since 2008.

It also is the first time in a decade the fed-funds rate will rise above inflation, measured by the Fed's preferred gauge, which excludes **volatile** energy and food categories. So-called core prices rose 2% in July.

"These rates remain low," Fed Chairman Jerome Powell said at a news conference. "This gradual return to normal is helping to sustain this strong economy for the longer-run benefit of all Americans."

Mr. Trump, at a news conference later Wednesday, said he was "not happy" about the Fed raising rates. But he said, "They are raising them because we are doing so well." And he said higher rates weren't all bad because they could help people who rely on interest savings for income.

Mr. Powell said the central bank decision was guided by economic theory and evidence -- not politics: "That's who we are. That's what we do. And that's just the way it's always going to be for us," he said.

Stocks erased gains and closed lower Wednesday. The **S&P 500** fell 0.3%. The yield on the benchmark 10-year U.S. Treasury note fell 3.059% from 3.102%. Yields fall as **bond prices** rise, and Treasury yields are near their highest levels in seven years.

The Fed's actions ripple through the economy over time by raising borrowing costs for businesses and consumers. Rising mortgage rates appear to have contributed to a somewhat slower pace of home sales this year.

Even if the Fed raises its benchmark rate to 3% next year, "we don't think that's a hindrance to the economy," said John Augustine, chief investment officer at Huntington Private Bank in Columbus, Ohio. "We don't see that lifting mortgage rates substantially. We don't see that as a threat to credit line borrowing."

The big question now is how much higher officials think they need to raise rates to keep the economy from overheating. The Fed targets a 2% inflation rate, which it sees as a sign of healthy demand. It wants to avoid economic growth that becomes unsustainable, leading to a boom and then bust.

Projections released after Wednesday's meeting show that most Fed officials expect they will raise rates by 1 percentage point through next year, and most officials penciled in at least one more quarter-point increase for 2020.

That would leave the benchmark rate slightly higher than 3.25%. Because this is modestly above the so-called neutral rate most officials project is required to balance supply and demand over the long run, such a setting would deliberately restrict growth.

Mr. Powell has stressed the uncertainty of estimating this neutral setting. To that end, the Fed dropped from its postmeeting statement on Wednesday a sentence that for years had described its rate stance as "accommodative," meaning officials were pressing on the gas pedal to spur more growth.

Economic projections released after the meeting envision an unusually favorable set of conditions in which the unemployment rate holds below 4% over the next three years but inflation never rises far beyond the Fed's 2% target.

Whether the Fed realizes this "Goldilocks" economy that is neither too hot nor too cold could depend on whether inflation behaves as expected.

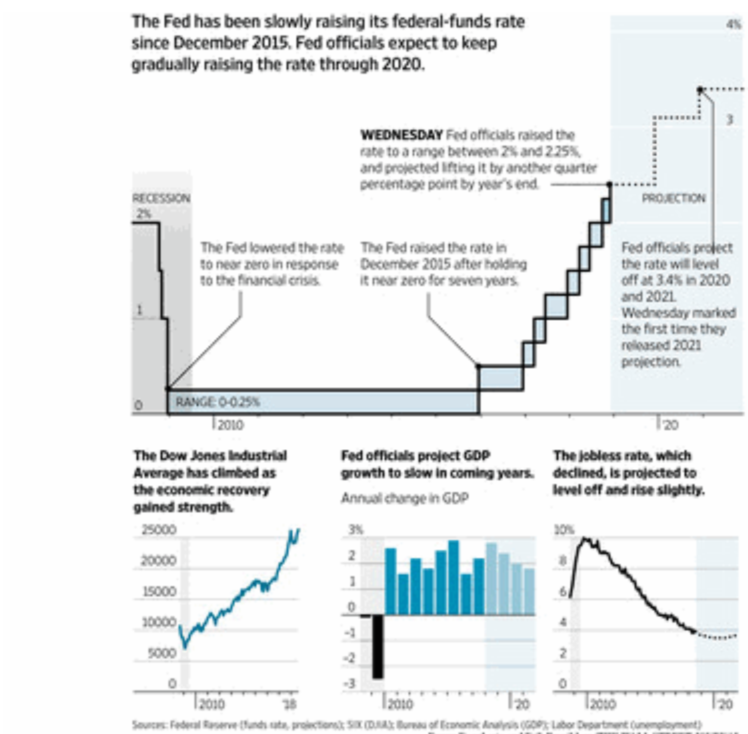
The risk that inflation climbs higher and faster than anticipated could require the Fed to raise rates "a little bit quicker," Mr. Powell said. He quickly added, "We don't see that. We really don't see that."

Wednesday's interest-rate projections show two different schools of thought about how the Fed might proceed.

One camp of officials said so long as unemployment keeps falling farther below the level they project is consistent with low and stable inflation, the Fed will need to raise rates to prevent the economy from overheating. This is an uncontroversial strategy because it is what the central bank always does at this point in an expansion.

Another camp argues for a relatively radical departure from this norm. These officials have said if inflation doesn't appear to be accelerating beyond 2%, the Fed could stop raising rates after reaching a neutral setting that neither spurs nor slows growth.

The Fed's projection that the economy could stay in a sweet spot for years also depends on forces outside of its control, including trade policy.

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THE WALL STREET JOURNAL.
U.S. EDITION

Heard on the Street
**Rates Are Rising No Matter What**

By Justin Lahart
392 words
27 September 2018
The Wall Street Journal
J
B13
English


[Financial Analysis and Commentary]

Worried about the Federal Reserve's rate-raising campaign? With the economy strong and unemployment extremely low, it would have been more worrisome if the Fed had left rates where they were.

In a well telegraphed decision, the Fed on Wednesday raised its target range on overnight rates by a quarter point, marking its third rate increase of the year. And it signaled that it plans to raise rates once more this year, and three times next year.

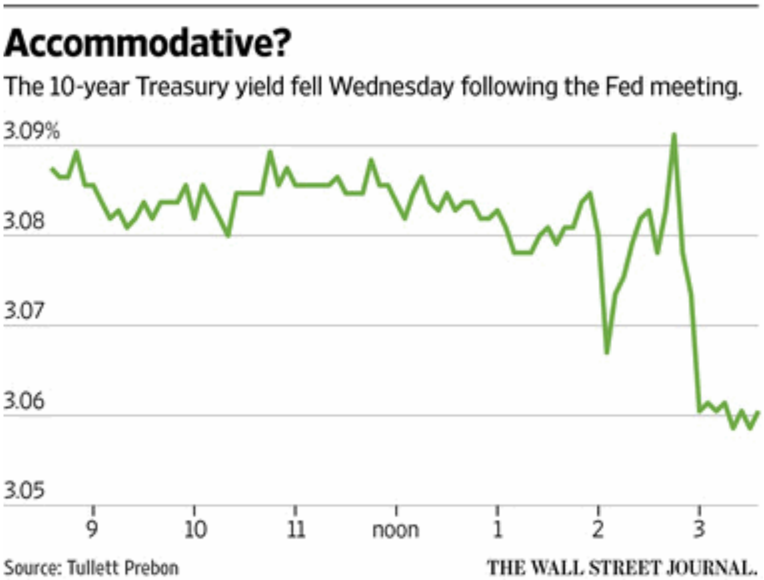
But despite its plans to keep on raising rates, policy makers in their postmeeting statement removed a phrase describing policy as accommodative. On the face of it, that seems strange. When rates increase to the point they aren't accommodative, they would first become neutral, meaning they aren't juicing or slowing the economy. So if they are neutral, why would the Fed be planning to raise them by a full point over the next year?

The truth is Fed officials dropped "accommodative" not because they don't want to use the word "neutral," but because they, and Fed Chairman Jerome Powell in particular, are trying to get away from the idea that they precisely know where neutral is. Mr. Powell took pains to explain that during his postmeeting news conference, pointing out that every policy maker said that they expect interest rates over the long run to be above current levels -- an indication that, policy makers think the current level of rates really is accommodative.

Not that investors should need the Fed to tell them that. Pushed along by growing confidence, lower taxes and increased government spending, the economy is growing strongly. Absent more rate increases, it is easy to imagine the unemployment rate falling through 3%, and for inflation and **financial-market** excesses to start causing serious problems.

So the Fed is going to keep raising rates, and will stop not when they reach some preconceived right level but once the increases start to affect the economy and the dangers of overheating are allayed.

One risk is that by the time those signs emerge, the Fed will have raised rates by too much, but at this point that might be better than the alternative of keeping rates too low.

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Document J000000020180927ee9r00017

 

THE WALL STREET JOURNAL.
U.S. EDITION

**Index Firms Upgrade China --- FTSE Russell, MSCI move to increase sway of mainland stocks in products**

By Shen Hong in Shanghai and Saumya Vaishampayan in Hong Kong
607 words
27 September 2018
The Wall Street Journal
J
B11
English


Two major index providers took steps to boost the influence of mainland Chinese stocks in their widely tracked global benchmarks from next year -- a vote of confidence in a market that has been battered by trade and economic concerns.

The actions by FTSE Russell and MSCI Inc. partly reflect how much easier it has become to buy and sell these stocks through a trading link with Hong Kong. The changes could also bring hundreds of smaller Chinese companies to the attention of international money managers for the first time.

FTSE Russell said Wednesday evening U.S. time it will include domestic Chinese shares in its flagship emerging-market index in stages starting next June. Based on current prices, the move means mainland-listed companies will make up more than 5.5% of the benchmark in March 2020. It estimates this will bring in about $10 billion from passive investors, whose investments closely follow set benchmarks.

"This is a big step for the Chinese market," said Mark Makepeace, chief executive of FTSE Russell, in an interview. He said the change had been supported by major global investors, but added: "Given the size that the China market will represent in their global portfolios, they want developed market standards. It will take time to achieve that."

FTSE Russell, a unit of London Stock Exchange Group PLC, now classifies mainland Chinese shares as "secondary emerging," along with those of countries like Russia, India and Chile. It already offers other benchmarks that include domestic Chinese stocks.

Earlier, rival MSCI proposed sharply increasing the importance of mainland Chinese stocks in its own influential global indexes next year. If it goes ahead, mainland-listed companies could make up 2.8% of the widely tracked MSCI Emerging Index by August 2019 and 3.4% by May 2020, up from about 0.7% now.

"This reflects the broader trend of global investors getting keener to include Chinese assets in their portfolios, because after all we have strong companies that are only listed domestically," said Jacky Zhang, a Shanghai-based analyst at BOC International.

Foreign investors' increasing appetite for Chinese shares is notable in an otherwise dismal year for the country's stock markets. With domestic investors worried about escalating trade tensions with the U.S., the Shanghai Composite Index has fallen 15% in the year to date as of Thursday morning in China.

Chinese companies' contribution to MSCI indexes is capped at just 5% of the market value of their freely traded shares, whereas for more established markets such as South Korea, the inclusion factor is 100%. In a statement late Tuesday, MSCI proposed quadrupling this cap to 20% -- in two steps -- in May and August 2019.

Full inclusion will probably take five years and could bring about $350 billion more into China, UBS Global Wealth Management has estimated.

Similarly, by March 2020, FTSE Russell will include Chinese firms at 25% of their "investability weight" -- a measure of the shares that can be owned by foreigners, given a company's free float and any restrictions on foreign ownership.

FTSE Russell's selection will include midcap and small-cap companies, as well as those with large market values. Meanwhile, MSCI said it was looking to add midsize stocks in 2020 and proposed making stocks listed on Shenzhen's ChiNext, a **Nasdaq**-style board that is heavy with tech firms, eligible for the index beginning in May.

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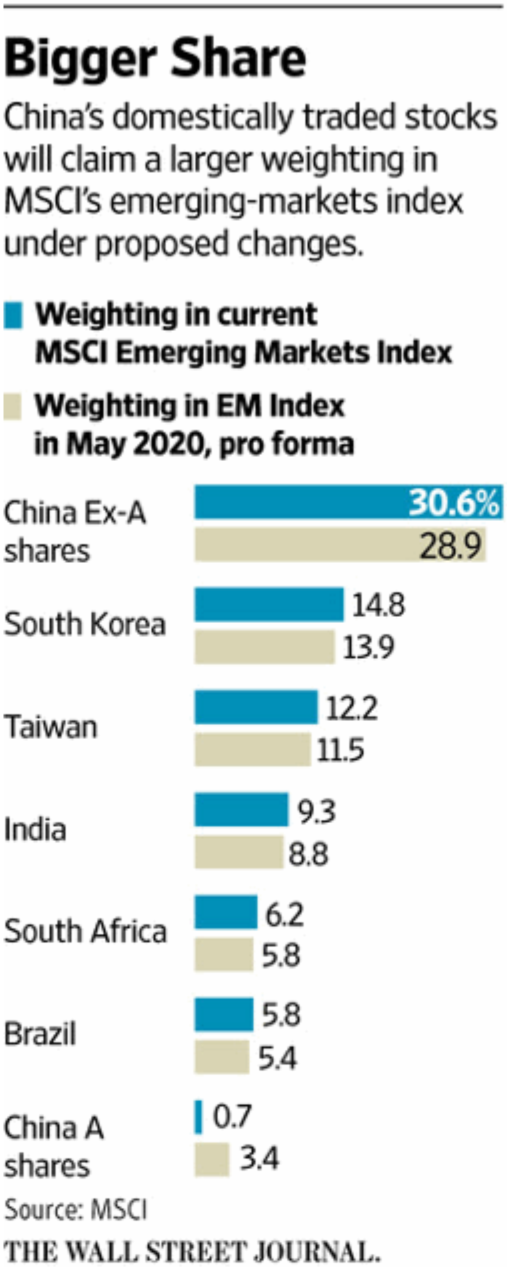
Quentin Webb contributed to this article.

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THE WALL STREET JOURNAL.
U.S. EDITION

**Lawsuit Against New York Fed Seen As a Policy Threat**

By Michael S. Derby
692 words
27 September 2018
The Wall Street Journal
J
B11
English


A lawsuit against the Federal Reserve Bank of New York could complicate the central bank's effort to control short-term interest rates at a time investor scrutiny of those markets is intensifying.

TNB USA Inc. contends in a federal suit filed in late August that it has been wrongly blocked in its pursuit of a "master account" at the Fed that would allow it to earn interest on deposits placed on the Fed's books.

Analysts say that if TNB won approval to offer deposit accounts to clients and other banks copy its model, the development could pose a threat to how the Fed has controlled short-term rates since the 2008 crisis.

Instead of targeting a specific short-term rate, as it did before the financial meltdown, the Fed now sets a firm range between the rate it will pay deposit-taking banks at the high end and the overnight reverse repurchase rate that is available to an approved roster of money managers and other institutions at the low end. The fed-funds rate floats in between.

TNB and other banks like it could thwart this system, analysts said, by collecting interest at the higher rate and offering that rate, minus a spread to cover costs and profits, to institutions that deposit money with them.

"I applaud the cleverness of this," said Tim Duy, an economics professor at the University of Oregon. "That spread was sitting out there and somebody found a way to take advantage of that."

The Fed's range for the funds rate now stands at between 2.00% and 2.25%, with the interest on excess reserves rate at 2.20%, following the conclusion of its interest-rate-setting meeting Wednesday.

TNB and banks like it would allow the sort of firms that would otherwise earn the lower reverse repo rate a way to get a higher return. That could render the rate floor moot.

The Fed would still have a lot of control over short-term rates, but the lower-end floor could cease to be a meaningful rate.

Some Fed watchers say the threat to the rate-control regime may not prove that big a deal. For some time now, there has been little actual interest from eligible firms to earn the reverse repo rate, as those firms have put their money to work in other places, with better returns.

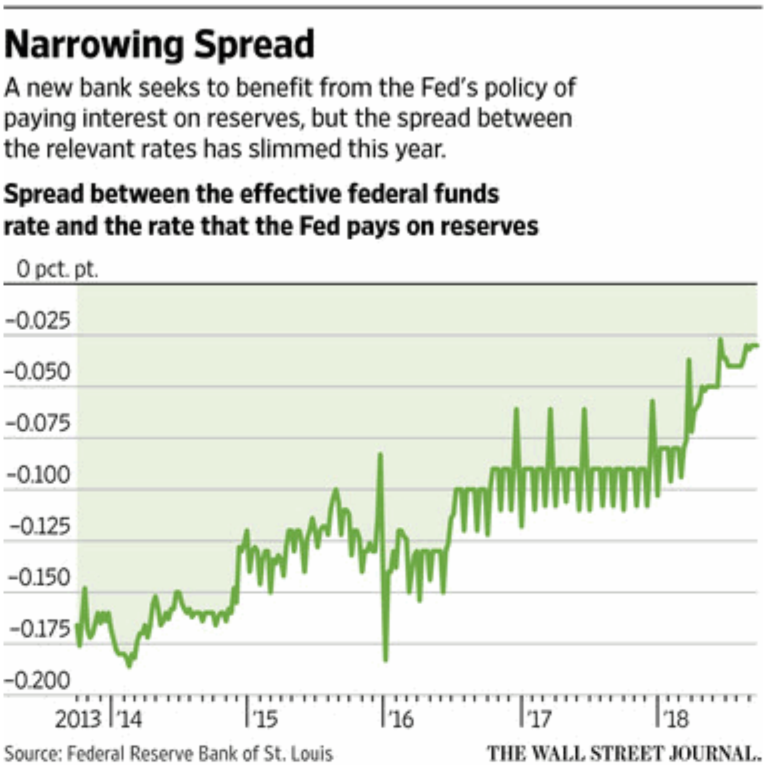
Regardless of market conditions, TNB says it isn't trying to break the system, and it has explained to the Fed how it will limit its activities to accomplish that. The Fed "has a clear statutory obligation" to grant the official account, said James McAndrews, a former Fed research official who is leading TNB. He also believes the TNB model is entirely complementary to the Fed's monetary-policy goals and reinforces what is now in place.

The Fed hasn't said why it hasn't approved TNB's application beyond unspecified policy concerns, TNB's lawsuit says. Central-bank watchers say the denial is essentially without precedent. TNB is operating under a temporary charter that Connecticut banking regulators granted in August 2017 that expires next year.

The New York Fed so far hasn't responded to the suit, and it and the Fed's Board of Governors declined to address the claims.

There are longer-term implications of the TNB model. If it proves popular -- and there is no way to know yet whether it would -- it could serve as the first step on a longer march to connect the public to the central bank more directly. Some academics have argued monetary policy could be made more potent if people and companies were allowed to bank directly with the Fed via interest-bearing accounts.

Fed policy changes could then bypass fickle **financial markets** and make themselves felt at the consumer level, which would in theory make rate changes more powerful. TNB may not be seeking such an outcome, but a successful performance of its model could start the wheels turning for such a world.

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WSJ PRO CENTRAL BANKING

Economy

**Bank Indonesia Raises Rates Again; The central bank raised the benchmark seven-day reverse repo rate by a quarter of a percentage point to 5.75%**

By I Made Sentana
398 words
27 September 2018
04:44 AM
WSJ Pro Central Banking
RSTPROCB
English


JAKARTA—Bank Indonesia on Thursday raised interest rates for the fifth time since May, and said it would introduce trade in domestic non-deliverable forwards for the rupiah to reduce exchange-rate **volatility**.

The central bank raised the benchmark seven-day reverse repo rate by a quarter of a percentage point to 5.75% after the U.S. Federal Reserve tightened its policy rate by a quarter point overnight.

"(The rate increase) is to reduce the current-account deficit to the sustainable level and maintain the attractiveness of our capital market," Bank Indonesia Governor Perry Warjiyo said.

Eleven of the 14 economists surveyed by The Wall Street Journal predicted the central bank would raise borrowing costs, with many citing the prevention of further outflows as the main reason.

Bank Indonesia has been one of Southeast Asia's most aggressive central banks so far this year, given that the rupiah has been among the region's worst performers.

The rupiah has weakened by 9% against the dollar this year, hurt by the Fed's policy normalization, the meltdown in other emerging markets' currencies, and U.S.-China trade tensions.

Mr. Warjiyo added the central bank will introduce domestic non-deliverable forward rupiah trading for investors and companies who wish to hedge their exchange-rate exposure.

"The objective is to support rupiah stability, increase the liquidity and efficiency of the domestic foreign exchange market, and mitigate exchange rate risks," Mr. Warjiyo said.

The domestic NDFs will be available only to those with genuine hedging needs, such as foreign investors who hold rupiah bonds or shares. The contracts must be settled in the local currency.

Currently, dollar-rupiah NDF transactions are only available outside Indonesia, mostly in Singapore. Bank Indonesia said the offshore NDF transactions were made by speculators as well as genuine investors.

The onshore spot market usually tracks the offshore NDF market, especially during times when there is heavy selling on the local currency.

But it remains unclear when such trades will begin, as Bank Indonesia is still waiting for approval from the Ministry of Law and Human Rights and for participating banks to be ready.

Write to I Made Sentana at i-made.sentana@wsj.com

Document RSTPROCB20180927ee9r00001

The New York Times

Business/Financial Desk; SECTB
**Markets Dip After the Fed's Decision**

By THE ASSOCIATED PRESS
751 words
27 September 2018
The New York Times
NYTF
Late Edition - Final
7
English


Stock indexes dipped Wednesday after the United States Federal Reserve took the latest step in its campaign to pull interest rates gradually higher.

The decision to raise the federal funds rate for a third time this year was widely expected, and stocks initially climbed following the announcement. But the gains faded in the last 30 minutes of trading after Fed Chairman Jerome Powell finished speaking at a news conference. The sharpest losses came from financial stocks, hurt by a drop in Treasury yields, which can crimp lending profits for banks.

The **Standard & Poor's 500**-**stockindex** fell 9.59 points, or 0.3 percent, to 2,905.97 after being up as much as 0.5 percent earlier in the day. The **Dow Jonesindustrial average** fell 106.93, or 0.4 percent, to 26,385.28, and the **Nasdaq composite** lost 17.11, or 0.2 percent, to 7,990.37.

Powell said that the United States economy is in a ''particularly bright moment,'' which would point to continued increases in rates. But he also said that inflation does not seem likely to spike, which would allow the Fed to continue on its gradual path to raise rates off the record lows they set following the 2008 financial crisis.

Investors spent the most energy Wednesday parsing a phrase that the Fed dropped from its written statement following its rate decision, one that has been included for years, about how the central bank is being ''accommodative'' and keeping rates low. Did that mean the Fed would shade toward being less aggressive or more?

But Powell said in the press conference that losing the phrase was not a signal of any change in policy expectations.

Investors closely follow every clue about interest rates, which affect the flow of money and the broad economy, because high rates in the past have been the death knell for economic expansions and bull runs for stocks. But analysts say markets can continue to climb as long as this rise in rates is gradual.

''We have more room to run in this economic cycle,'' said Jon Adams, senior investment strategist for BMO Global Asset Management.

The Fed indicated Wednesday that it expects to raise rates one more time this year, three times in 2019 and once in 2020.

Treasury yields dipped on Wednesday, a step back from their steady rise this year.

The yield on the **10**-**year Treasury** note fell to 3.05 percent from 3.10 percent late Tuesday. It had been close to its highest level since 2011. The two-year Treasury yield, which more closely tracks movements by the Fed, dipped to 2.82 percent from 2.83 percent.

Brian Nick, chief investment strategist at Nuveen, said that it was puzzling that both stocks and bond yields fell following the Fed's move. Usually, when investors think the Fed is going to become more aggressive about raising interest rates, stocks fall but bond yields rise.

Nick said the reaction may be a result of the new 2021 forecasts the Fed gave for the unemployment rate and G.D.P. growth.

Among stocks in the **S**.**&P**. **500**, the biggest drop came from Cintas, which provides workers' uniforms, restroom supplies and other products to companies. The company reported better earnings for the latest quarter than analysts expected, but growth in rentals fell short of some forecasts. Cintas lost $11.80, or 5.5 percent, to $201.16.

On the winning side was SurveyMonkey's parent company, SVMK, which surged in its first day of trading. After pricing its initial public offering of stock at $12 per share, SVMK jumped as high as $20.00 during the morning. It closed at $17.24, up 43.7 percent.

Benchmark United States crude oil fell 1 percent to $71.57 per barrel.

Gold dropped $6.00 to $1,194.00 an ounce.

The dollar dipped to 112.85 Japanese yen from 112.93 yen late Tuesday. The euro slipped to $1.1744 from $1.1766, and the British pound fell to $1.3184 from $1.3186.

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 Wednesday. (Source: Reuters); New-Home Sales: Annual pace of new private homes sold during the month, seasonally adjusted. (Source: Commerce Department)

Document NYTF000020180927ee9r00056

 

The New York Times

Business/Financial Desk; SECT
**Here's One Emerging Threat That Could Derail the Bull Run**

By PETER EAVIS
607 words
27 September 2018
The New York Times
NYTF
The New York Times on the Web
English


Get the DealBook newsletter to make sense of major business and policy headlines -- and the power-brokers who shape them.

Nothing so far has succeeded in ending the bull run in stocks that began nearly a decade ago.

The rally survived the sluggish economy in the aftermath of the financial crisis, the European debt crises, fiscal battles in Washington, the oil bust, concerns about China's growth and, most recently, President Trump's trade war.

Now the **stock market** faces a more prosaic but nonetheless powerful threat: increasingly attractive returns on government bonds.

For years, yields on Treasuries were so low that investors had an incentive to buy stocks in the hope of higher returns. Yields are still quite low by historical standards, but they have been rising in recent weeks, and they could go even higher if the Federal Reserve keeps raising its target interest rate. (An increase was announced on Wednesday.)

The more yields go up, the more likely investors will choose the relative safety of Treasuries -- and that could cause the stock rally to stall. Warren E. Buffett has often commented on the connection between government bond yields and **stock market** investments. In a 1999 article in Fortune, Mr. Buffett said, "The rates of return that investors need from any kind of investment are directly tied to the risk-free rate that they can earn from government securities."

The yield on the **10**-**year Treasury** note has risen to 3.1 percent, from 2.4 percent at the end of last year, and analysts expect the yield to climb to 3.42 percent by the end of 2019, according to a Wall Street Journal survey. That yield is still far from beating the **stock market**'s recent annual performances. The **Standard & Poor**'**s** **500**-**stockindex** rose 19 percent last year and is up 9 percent this year. But buying a **10**-**year Treasury** today would provide its holders with 3 percent a year for a decade with virtually no risk of losing any money in the process.

Such a return might seem particularly attractive to investors who believe the **stock market** is expensive and is vulnerable to a sell-off. One way to make that comparison is to look at the difference between the yield on the **10**-**year Treasury** and the "yield" on the **stock market**, measured by dividing the historical yearly earnings of the **S**. **& P**. **500** companies by the value of the index. When the earnings yield is substantially higher than the **10**-**year Treasury** yield, investors are more likely to favor stocks. The difference has narrowed. It's now 1.83 percentage points, well below the 2.88-point average of the past three years.

If companies' profits continue to grow strongly, the earnings yield will rise and stocks will look more attractive compared with government bonds. But corporate earnings growth is expected to slow next year. And the trade war may cause corporate profits to moderate even more. In that case, the difference between the 10-year yield and the earnings yield would shrink even more. Investors may be more tempted then to shed stocks and put more money into bonds.

There is a major reason this **bearish** outcome may not occur. Profits could be stronger than analysts are forecasting.

But if companies disappoint investors with lackluster profits, the federal government has an investment it is eager to sell them.

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Document NYTF000020180927ee9r0004c

 

THE WALL STREET JOURNAL.

Markets

**Large Investors Dive Into Risky Loan Securities; Major Canadian pension plan investing $285 million in latest collateralized loan obligation purchase**

By Matt Wirz
791 words
26 September 2018
05:59 PM
The Wall Street Journal Online
WSJO
English


Corrections & Amplifications

Sound Point Capital Management's assets have grown by roughly 64% since April 2017 and the firm has 68 employees total. An earlier version of this article incorrectly stated the assets had grown by almost 70% and that the firm's CLO team had 68 employees. (Sept. 26, 2018)

Canada's government pension plan is investing $285 million in the riskiest securities of collateralized loan obligations, or CLOs, as large institutions start funneling more cash into a market that has received record sums in 2018.

The Canada Pension Plan Investment Board, or CPPIB, will buy equity in CLOs managed by Sound Point Capital Management, a New York-based credit hedge fund founded by former Bank of America investment banker Stephen Ketchum. It is the first such partnership for the pension, which sees CLO equity as an attractive way to boost returns on its leveraged loan investments, a plan spokesman said. CPPIB independently manages funds for 20 million Canadians who contribute to the plan.

CLOs raise money by issuing bonds and equity to outside investors and use the cash to buy bundles of below-investment-grade, or "leveraged," corporate loans. The money coming in from the bundled loans pays investors' interest and principal on the CLO bonds, in a process similar to mortgage-backed securitizations. Equity holders typically must cover loan losses above a certain threshold—an arrangement that accounts both for CLO equity's risk and for its higher expected returns.

CLO equity has historically been purchased by hedge funds or private-equity firms. Purchases by large institutions such as CPPIB, with $275 billion in assets, could give CLO managers significantly more firepower to launch new deals, further boosting demand for leveraged loans and potentially adding to risk in junk debt markets. Managers can borrow about $9 million of bonds for each $1 million of equity raised to buy up leveraged loan pools.

"The asset class has increasing acceptance from institutional investors," said Wade O'Brien, a managing director at Cambridge Associates who advises foundations and endowments on credit investments. Cambridge is recommending clients make investments in dedicated funds that buy only CLO equity, which can return about 15% annually in typical market conditions, he said.

The increased appetite for CLOs reflects a decadelong increase in purchases of junk-rated corporate and government debt by institutional investors in response to persistently low interest rates in safer markets. Purchases by CLOs helped push the leveraged-loan market to $1.22 trillion in June, exceeding the size of the junk bond market for the first time in 10 years.

The global CLO market has grown 25% in the past two years to about $700 billion outstanding, according to data from JPMorgan Chase & Co. Annual returns from the equity have averaged about 18% since 2004, according to research from JPMorgan, but some analysts caution that if leveraged loan defaults rise, certain CLOs will only have enough cash to keep paying their bonds, leaving equity holders with losses.

Institutional investors routinely purchased CLO bonds in recent years because they pay floating-rate interest—an advantage when interest rates are rising—and have outperformed more conventional corporate debt. CLO bonds rated single-B returned 38% in 2017 compared with 4.27% returned by comparable leveraged loans, according to data from Morgan Stanley.

CLO managers in the U.S. have raised about $100 billion so far this year, 24% more than in the same period of 2017, according to S&P Global, and analysts expect them to issue a record $130 billion or more in 2018. Sound Point's capital has surged by roughly 64% since April 2017 to $20 billion, driven principally by its CLO team, a company spokesman said.

That demand has pushed CLO **bond prices** higher and their yields lower— single-B CLO bonds have returned just 5.18% this year, according to data from Morgan Stanley—making CLO equity more attractive in comparison.

Analysts at Morgan Stanley said they are wary of CLO equity because leveraged loan prices could fall sharply, especially if concerns rise that loanholders will recover less when defaults rise than in prior downturns.

Many CLOs stopped paying equity holders in 2009 but resumed payments when loan prices rebounded unlike other structured investments that were completely wiped out in the financial crisis. CLO returns averaged about 6% in 2009 and 15% in 2010, said Rishad Ahluwalia, JP Morgan's head of CLO research. CLO securitizations fared far better than their mortgage-backed cousins in the crisis because leveraged loan defaults were far lower than in housing debt and no senior CLO bonds went unpaid.

Mr. Ahluwalia said many of the fund managers he has met with this year are mortgage securitization specialists looking to expand into CLO trading. "The CLO market has become very big," he said. "It's a market in its own right."

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THE WALL STREET JOURNAL.

Markets

**Bank Suit Could Complicate the Fed's Rate Policy; TNB contends it has been blocked in its effort to open an account at the Fed that would let it earn interest on deposits**

By Michael S. Derby
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A lawsuit against the Federal Reserve Bank of New York could complicate the central bank's effort to control short-term interest rates at a time when investor scrutiny of those markets is intensifying.

TNB USA Inc. contends in a federal suit filed in late August that it has been wrongly blocked in its pursuit of a "master account" at the Fed that would allow it to earn interest on deposits placed on the Fed's books.

Analysts say that if TNB won approval to offer deposit accounts to clients and other banks copied its model, the development could pose a threat to how the Fed has controlled short-term rates since the 2008 crisis.

Instead of targeting a specific short-term rate, as it did before the financial meltdown, the Fed now sets a firm range between the rate it will pay deposit-taking banks at the high end, and the overnight reverse repurchase rate that is available to an approved roster of money managers and other institutions at the low end. The fed-funds rate floats in between.

TNB and other banks like it could thwart this system, analysts said, by collecting interest at the higher rate and offering that rate, minus a spread to cover costs and profits, to institutions that deposit money with them.

"I applaud the cleverness of this," said Tim Duy, an economics professor at the University of Oregon. "That spread was sitting out there and somebody found a way to take advantage of that."

The Fed's range for the funds rate now stands at between 2.00% and 2.25%, with the interest on excess reserves rate at 2.20%, following the conclusion of its interest-rate setting meeting Wednesday.

TNB and banks like it would allow the sort of firms that would otherwise earn the lower reverse repo rate a way to get a higher return. That could render the rate floor moot. The Fed would still have a lot of control over short-term rates, but the lower end floor could cease to be a meaningful rate.

Some Fed watchers say the threat to the rate control regime may not prove that big a deal. For some time now, there has been little actual interest from eligible firms to earn the reverse repo rate, as those firms have put their money to work in other places, with better returns.

George Selgin, a Cato Institute senior fellow, attributes this situation in a blog post to "the tendency of the Fed's policy rate settings to lag further and further behind increases in market-determined interest rates" in a time of expanding budget deficits.

Regardless of market conditions, TNB says it isn't trying to break the system, and it is explained to the Fed how it will limit its activities to accomplish that. The Fed "has a clear statutory obligation" to grant the official account, said James McAndrews, a former Fed research official who is leading TNB. He also believes the TNB model is entirely complementary of the Fed's monetary policy goals and reinforces what's now in place.

The Fed hasn't said why it hasn't approved TNB's application beyond unspecified "policy concerns," TNB's lawsuit says. Central bank watchers say the denial is essentially without precedent. TNB is operating under a temporary charter that Connecticut banking regulators granted in August 2017 that expires next year.

The New York Fed has thus far not responded to the suit, and it and the Fed's Board of Governors declined to address the claims.

Peter Conti-Brown, a legal studies and business ethics professor at the Wharton School of the University of Pennsylvania, said he's "not convinced that the Fed has the legal authority to deny TNB its master account." The Fed "will have to show why it has the statutory authority to use discretion to deny" an application like TNB's, Mr. Conti-Brown said.

There are longer-term implications of the TNB model. If it proved popular—and there is no way to know yet whether it would—it could serve as the first step on a longer march to connect the public to the central bank more directly. Some academics have argued monetary policy could be made more potent if people and companies were allowed to bank directly with the Fed, via interest-bearing accounts.

Fed policy changes could then bypass fickle **financial markets** and make themselves felt at the consumer level, which would in theory make rate changes more powerful. TNB may not be seeking such an outcome, but a successful performance of its model could start the wheels turning for such a world.

TNB is "another manifestation of how innovation runs ahead of regulation," said David Beckworth, of George Mason University's Mercatus Center. "The Fed's fear is not only destroying the floor system, but moving their balance sheet one step closer to more and more entities and ultimately the public."

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THE WALL STREET JOURNAL.

Business
**SurveyMonkey Soars in Public Market Debut; The SaaS company's stock closed Wednesday up 44% from its initial offering price**

By Maureen Farrell and Kimberly Chin
515 words
26 September 2018
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The Wall Street Journal Online
WSJO
English


Shares of SVMK Inc., the parent company of SurveyMonkey, soared in their first day of trading Wednesday, indicating growing investor appetite for software services platforms and newly public technology companies.

The firm's stock, which is listed on the **Nasdaq** under the symbol SVMK, closed Wednesday at $17.24, a 44% jump from its initial offering price of $12, which was already above the range the company had set ahead of its roadshow to market shares to potential investors.

On Tuesday, SurveyMonkey's IPO, which was led by JPMorgan Chase & Co., Allen & Co. and Bank of America Corp., sold 15 million shares, generating $180 million in proceeds after the offering was boosted from an expected 13.5 million shares.

SurveyMonkey is the latest in a line of many tech companies that have made their debut recently to hot demand. Investors have sought the high growth of these firms, bidding up their IPO prices and then their shares on the first day of trading. Recently, Eventbrite Inc. and online luxury digital marketplace Farfetch Ltd. rose sharply in their public debuts.

U.S.-listed tech IPOs are trading on average up 49.8% this year from their IPO prices, far outpacing the broader market's gains this year, according to Dealogic data. U.S.-listed IPOs are up 26% on average, Dealogic data show.

The IPO "is a huge marketing event," SVMK's Chief Executive Zander Lurie said in an interview Wednesday. "If you feel like your team has the rigor and the accountability to deliver on those expectations, then it's a good opportunity to showcase it."

Ahead of the offering, the venture arm of Salesforce.com Inc. said it would also invest at the company's IPO price, amounting to a roughly $40 million investment. Mr. Lurie said investors "took comfort" from Salesforce's investment. "Really smart investors like to be surrounded with other folks who do diligence. I don't think anybody does a better job of product diligence than a company like Salesforce."

SVMK, a San Mateo, Calif.-based company that was founded in 1999, is a software-as-a-service platform that makes it easy for individuals and organizations to create their own online surveys. It is among a group of companies that have been around for more than a decade to tap a hot IPO market.

Mr. Lurie noted that none of the company's existing shareholders are selling stock in the IPO, signaling interest in the company's future.

In 2017, SurveyMonkey posted sales of $218.8 million, compared with $207.3 million in the previous year. Average revenue per user rose to $362, up from $349 compared with the year prior in 2016. For the first six months of this year, that figure was $400 up from $351 in the same period last year.

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# The New York Times

Business Day; DealBook
**Companies Can't Seem to Quit Quarterly Guidance: DealBook's Closing Bell**

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Get the DealBook newsletter to make sense of major business and policy headlines — and the power-brokers who shape them.__________

Calls for companies to eliminate quarterly earnings guidance are growing, but so is the number of companies issuing them. Warren E. Buffett, the head of Berkshire Hathaway, Jamie Dimon, the chief executive of JPMorgan Chase, and Laurence D. Fink, the chief executive of BlackRock, have all criticized quarterly guidance. They have said it hinders a company's ability to achieve long-term goals and should be ended. But last year, 146 companies in the **Standard & Poor's 500-stockindex** provided earnings guidance 444 times, according to S & P Global Market Intelligence. That was the highest number in a decade, and the pace doesn't appear to have slowed much this year. As of Sept. 12, 128 companies in the **S**. **& P**. **500** had provided quarterly guidance 321 times.

If Federal Reserve policy is no longer accommodative, then what is it? Since the financial crisis, the central bank had described monetary policy as accommodative. But the word was dropped from Wednesday's policy statement. That's an indication that the Fed's benchmark interest rate is rising back to a level that it regards as neutral or, in other words, neither stimulating nor restraining economic growth. Some have speculated that the removal of the language would be a dovish signal. But at a news conference Wednesday, the Fed chairman, Jerome H. Powell, said: "The change does not signal any change in the likely path of policy. Instead, it is a sign that policy is proceeding in line with our expectations."

The Fed and trade. As it sets monetary policy, the Fed is monitoring the effect on the economy of President Trump's trade measures, which include tariffs on steel and aluminum as well as a wide range of imports from China. The tariffs could push up costs for companies and consumers and make it harder for United States exporters as other countries retaliate. During the news conference, Mr. Powell sounded more concerned about the economic consequences of the trade battle than he had at past meetings: "We've been hearing a rising chorus of concerns from businesses all over the country about the disruption of supply chains, materials costs increases and loss of markets." But Mr. Powell said the Fed had not seen much evidence in the numbers that the trade tensions were harming the economy. "It's hard to see much happening at this point," he said. Mr. Powell warned, however, about a situation in which tariffs remained in place for a long time and the world became more protectionist. "That's going to be bad for the United States economy and American workers and families, and also for other economies," he said.

Could Live Nation Entertainment be next on SiriusXM's shopping list? The satellite radio provider agreed to acquire the music streaming service Pandora Media for $3.5 billion on Monday. "This transaction is likely the first of multiple deals involving SiriusXM, particularly as the all-stock nature of the Pandora acquisition did nothing to address Sirius's growing access to cash," said Brandon Ross, an analyst at BTIG. He said he continued to believe that SiriusXM's controlling shareholder, Liberty Media, "wishes to eventually control a combined SiriusXM, Pandora and Live Nation."

At what point do higher **oil prices** weigh on the economy? Oil has been a better bet this year than stocks — even technology stocks. Of course, rising **oil prices** historically have not been good for the United States economy. So with oil up around 20 percent this year, some have begun to wonder when it will become a drag on the economy. "**Oil prices** need to double in a year or less before they trigger a recession," said Nicholas Colas, a co-founder of DataTrek Research. That means crude oil needs to climb above $100 a barrel before the end of the year. It currently trades around $71.

Warren E. Buffett, left, and Jamie Dimon, center, are among the business leaders who favor eliminating quarterly earnings guidance. | Donald Bowers/Getty Images for Fortune

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International New York Times

business
**As Debt Rises, the Government Will Soon Spend More on Interest Than on the Military**

By NELSON D. SCHWARTZ
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English


The federal government could soon pay more in interest on its debt than it spends on the military, Medicaid or children's programs.

The run-up in borrowing costs is a one-two punch brought on by the need to finance a fast-growing budget deficit, worsened by tax cuts and steadily rising interest rates that will make the debt more expensive.

With less money coming in and more going toward interest, political leaders will find it harder to address pressing needs like fixing crumbling roads and bridges or to make emergency moves like pulling the economy out of future recessions.

Within a decade, more than $900 billion in interest payments will be due annually, easily outpacing spending on myriad other programs. Already the fastest-growing major government expense, the cost of interest is on track to hit $390 billion next year, nearly 50 percent more than in 2017, according to the Congressional Budget Office.

"It's very much something to worry about," said C. Eugene Steuerle, a fellow at the Urban Institute and a co-founder of the Urban-Brookings Tax Policy Center in Washington. "Everything else is getting squeezed."

Gradually rising interest rates would have made borrowing more expensive even without additional debt. But the tax cuts passed late last year have created a deeper hole, with the deficit increasing faster than expected. A budget bill approved in February that raised spending by $300 billion over two years will add to the financial pressure.

The deficit is expected to total nearly $1 trillion next year — the first time it has been that big since 2012, when the economy was still struggling to recover from the financial crisis and interest rates were near zero.

Deficit hawks have gone silent, even proposing changes that would exacerbate the deficit. House Republicans introduced legislation this month that would make the tax cuts permanent.

"The issue has just disappeared," said Senator Mark Warner, a Virginia Democrat. "There's collective amnesia."

The combination, say economists, marks a journey into mostly uncharted financial territory.

In the past, government borrowing expanded during recessions and waned in recoveries. That countercyclical policy has been a part of the standard Keynesian toolbox to combat downturns since the Great Depression.

The deficit is soaring now as the economy booms, meaning the stimulus is pro-cyclical. The risk is that the government would have less room to maneuver if the economy slows.

Aside from wartime or a deep downturn like the 1930s or 2008-9, "this sort of aggressive fiscal stimulus is unprecedented in U.S. history," said Jeffrey Frankel, an economist at Harvard.

Pouring gasoline on an already hot economy has resulted in faster growth — the economy expanded at an annualized rate of 4.2 percent in the second quarter. But Mr. Frankel warns that when the economy weakens, the government will find it more difficult to cut taxes or increase spending.

Lawmakers might, in fact, feel compelled to cut spending as tax revenue falls, further depressing the economy. "There will eventually be another recession, and this increases the chances we will have to slam on the brakes when the car is already going too slowly," Mr. Frankel said.

Interest costs make it harder for the government to do other things

Finding the money to pay investors who hold government debt will crimp other parts of the budget. In a decade, interest on the debt will eat up 13 percent of government spending, up from 6.6 percent in 2017.

“By 2020, we will spend more on interest than we do on kids, including education, food stamps and aid to families,” said Marc Goldwein, senior policy director at the Committee for a Responsible Federal Budget, a research and advocacy organization.

Interest costs already dwarf spending on many popular programs. For example, grants to students from low-income families for college total roughly $30 billion — about one-tenth of what the government will pay in interest this year. Interest payments will overtake Medicaid in 2020 and the Department of Defense budget in 2023.

What’s more, the heavy burden of interest payments could make it harder for the government to repair aging infrastructure or take on other big new projects.

Mr. Trump has called for spending $1 trillion on infrastructure, but Congress has not taken up that idea.

The U.S. hasn’t faced this issue for years

Until recently, ultralow interest rates, set by the Federal Reserve to support the economy, allowed lawmakers to borrow without fretting too much about the cost of that debt.

But as the economy has strengthened, the Fed has gradually raised rates, starting in December 2015. The central bank is expected to push rates up again on Wednesday, and more increases are in store.

“When rates went down to record lows, it allowed the government to take on more debt without paying more interest,” Mr. Goldwein said. “That party is ending.”

Since the beginning of the year, the yield on the **10**-**year Treasury** note has risen by more than half a percentage point, to 3.1 percent. The Congressional Budget Office estimates that the yield will climb to 4.2 percent in 2021. Given that the total public debt of the United States stands at nearly $16 trillion, even a small uptick in rates can cost the government billions.

There’s no guarantee that these forecasts will prove accurate. If the economy weakens, rates might fall or rise only slightly, reducing interest payments. But rates could also overshoot the budget office forecast.

Some members of Congress want to set the stage for even more red ink. Republicans in the House want to make last year’s tax cuts permanent, instead of letting some of them expire at the end of 2025. That would reduce federal revenue by an additional $631 billion over 10 years, according to the Tax Policy Center.

No, the United States isn’t at risk of becoming the next Greece

Deficit hawks have warned for years that a day of reckoning is coming, exposing the United States to the kind of economic crisis that overtook profligate borrowers in the past like Greece or Argentina.

But most experts say that isn’t likely because the dollar is the world’s reserve currency. As a result, the United States still has plenty of borrowing capacity left because the Fed can print money with fewer consequences than other central banks.

And interest rates plunged over the last decade, even as the government turned to the market for trillions each year after the recession. That’s because Treasury bonds are still the favored port of international investors in any economic storm.

“We exported a financial crisis a decade ago, and the world responded by sending us money,” said William G. Gale, a senior fellow at the Brookings Institution.

But that privileged position has allowed politicians in both parties to avoid politically painful steps like cutting spending or raising taxes.

That doesn’t mean rapidly rising interest costs and a bigger deficit won’t eventually catch up with us.

Charles Schultze, chairman of the Council of Economic Advisers in the Carter administration, once summed up the danger of deficits with a metaphor. “It’s not so much a question of the wolf at the door, but termites in the woodwork.”

But Washington doesn’t want to hear about the potential problems

Rather than simply splitting along party lines, lawmakers’ attitudes toward the deficit also depend on which party is in power. Republicans pilloried the Obama administration for proposing a large stimulus in the depths of the recession in 2009 and complained about the deficit for years.

In 2013, Senator Mitch McConnell of Kentucky called the debt and deficit “the transcendent issue of our era.” By 2017, as Senate majority leader, he quickly shepherded the tax cut through Congress.

Senator James Lankford, an Oklahoma Republican who warned of the deficit’s dangers in the past, nevertheless played down that threat on the Senate floor as the tax billed neared passage.

“I understand it’s a risk, but I think it’s an appropriate risk to be able to say let’s allow Americans to keep more of their own money to invest in this economy,” he said.

He also claimed the tax cuts would pay for themselves even as the Congressional Budget Office estimated that they would add $250 billion to the deficit on average from 2019 to 2024.

In an interview, Mr. Lankford insisted that the jury was still out on whether the tax cuts would generate additional revenue, citing the strong economic growth recently.

While the Republican about-face has been much more striking, Democrats have adjusted their position, too.

Mr. Warner, the Virginia Democrat, called last year’s tax bill “the worst piece of legislation we have passed since I arrived in the Senate.” In 2009, however, when Congress passed an $800 billion stimulus bill backed by the Obama administration, he called it “a responsible mix of tax cuts and investments that will create jobs.”

The difference, Mr. Warner said, was that the economy was near the precipice then.

“There was virtual unanimity among economists that we needed a stimulus,” he said. “But a $2 trillion tax cut at the end of a business cycle with borrowed money won’t end well.”

PHOTO: Interest payments, already the fastest-growing major government expense, are on pace to surpass military spending in 2023. (PHOTOGRAPH BY JEON HEON-KYUN/EPA, VIA SHUTTERSTOCK) (A13) CHART: Payments Projected to Top $900 Billion Annually, and That's Not Even for Principal (Source: Congressional Budget Office) (A13)

* Trump Administration Mulls a Unilateral Tax Cut for the Rich

* How the Trump Tax Cut Is Helping to Push the Federal Deficit to $1 Trillion

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**Health-Care Stocks Take Rally's Lead**

By Michael Wursthorn
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26 September 2018
The Wall Street Journal
J
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English


Health-care stocks have emerged as market leaders in the third quarter, helping push major U.S. indexes to new highs.

One reason: Money managers are embracing the sector as a safety play, particularly after big technology stocks stumbled in September.

The health-care sector is the best performer of the **S&P 500**'s 11 groups in the third quarter, up 13% and on pace for its strongest showing in more than five years. On a year-to-date basis, health-care stocks are trailing only the technology and consumer-discretionary sectors.

Hedge funds have built up their biggest position in health-care shares in the past five years. About 17% of their assets are in the sector, second only to shares of tech companies, according to Goldman Sachs Group Inc. data through June. Mutual-fund managers also have been shifting into health-care stocks, with many building outsize positions, according to Goldman's data.

And flows into health-care-focused mutual funds and exchange-traded funds, popular with retail investors, are at their strongest in three years, according to Morningstar Inc.

Rising interest in the stocks coincides with surging profits across the industry. Plus, the health-care needs of an aging population are expected to insulate the companies from a downturn, and investors searching for attractively valued stocks after a nine-year **bull market** in the U.S. have embraced the shares.

The sector's rally has been broad, with shares of pharmaceutical giants such as Merck & Co. and Pfizer Inc., insurers including Humana Inc. and UnitedHealth Group Inc., and equipment suppliers like Abiomed Inc. and Align Technology Inc. all rising at least 20% in 2018.

"These stocks had been out of favor for a while," said Tom Hancock, head of focused equity at Grantham, Mayo, Van Otterloo & Co., or GMO, a Boston-based money-management firm. "But we've been trying to find stocks that aren't being inflated by this rising tide of economic good news," he added, referring to the strong U.S. growth that has helped fuel a broad **stock-market** upswing in recent years. "When that tide recedes, we're looking for companies that will be OK in that environment."

Big tech stocks have led much of this year's rally, including Amazon.com Inc., Google parent Alphabet Inc. and Apple Inc., which each fell more than 3% in September. Investors have cut their exposure amid concerns about new regulations in the wake of Facebook Inc.'s data mishap.

At firms like GMO, investors have been trimming their technology holdings to help fund their shifts into health care. GMO's funds recently initiated a position in Merck, Mr. Hancock said, as it has focused on further developing cancer-treatment drug Keytruda. Merck shares have surged 26% this year and 16% in the third quarter alone.

GMO funds, meanwhile, trimmed stakes in Alibaba Group Holding Ltd. and Microsoft Corp. in the past six months, according to FactSet.

Similarly, hedge-fund manager Tudor Investment Corp. increased its stake in health insurer Aetna Inc. and initiated new positions in drugmakers Shire PLC and AbbVie Inc. all in the past six months, according to fund-holdings data compiled by FactSet. Millennium Management LLC, another hedge fund, added to its positions in medical-device makers Medtronic PLC and Boston Scientific Corp.

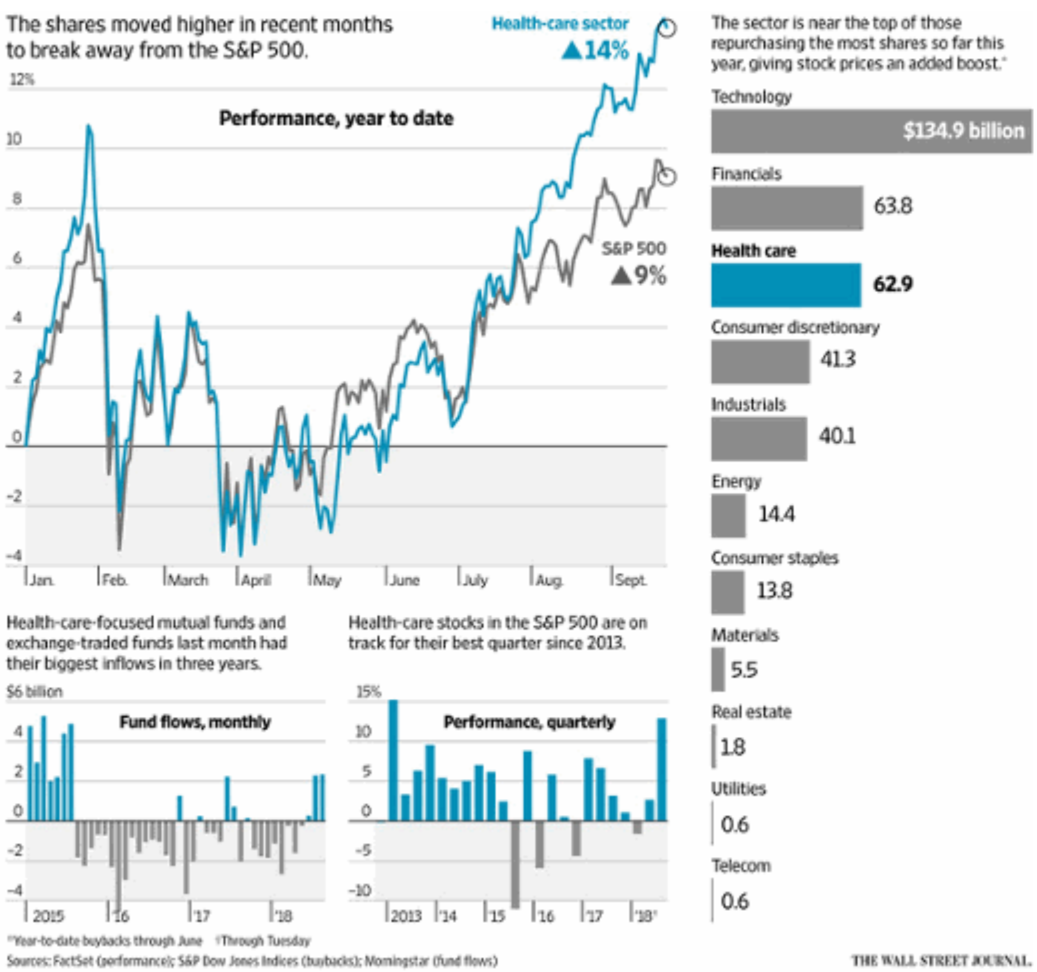
Tudor declined to comment through a spokesman. Millennium didn't respond to a request for comment.

Some investors, though, question the timing of health care's sudden appeal, citing its bouts of volatility when political debates over how Americans pay for health care intensify. The sector will likely see another jolt should Republicans retain control of Congress in November's midterm elections and resume talks of a health-care overhaul, said Lewis Piantedosi, a vice president and portfolio manager for Eaton Vance Management, which has kept its allocation toward health-care stocks below its benchmark.

Still, the broader shift into health-care stocks suggests investors are eschewing risk after a long rally.

Investors tend to view health-care stocks as a defensive investment because health insurers, pharmaceutical companies and medical-device makers usually hold up better in times of economic turbulence. That is because most medical expenses can't be put off in a recession, and economic swings don't typically curb the rollout of new drugs and devices. Valuations are also enticing, investors said, with health-care stocks in the S&P 500 trading in line with the broader S&P 500 at about 17 times future earnings, compared with 18 times for the tech sector and 23 times for consumer-discretionary companies, according to FactSet.

"Not to say it can't continue, but we're in the longest bull market ever," said Matthew Watson, a portfolio manager at James Advantage Funds. "So from a risk standpoint, getting into health-care stocks, which tends to be defensive, makes sense for us, too."

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THE WALL STREET JOURNAL.
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Heard on the Street
**Oil's Ascent Above $80 a Barrel Is Bruising for Turkey**

By Jon Sindreu
415 words
26 September 2018
The Wall Street Journal
J
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English


[Financial Analysis and Commentary]

In the U.S., oil above $80 a barrel is an annoyance for drivers. In Turkey, it could tip the entire economy into recession.

Sunday's decision by major oil producers to keep output steady has pushed international **oil prices** to their highest level since November 2014 in dollar terms. In Turkish lira, the **oil price** is the most expensive ever, having almost doubled so far this year.

The lira has found a firmer footing since officials jacked interest rates up to 24% this month. But it is still down roughly 38% against the U.S. dollar this year, hurt by concerns about the Turkish central bank's lack of independence as well as unsustainable debts taken on by domestic companies and banks.

Faced with a weaker lira, Turks are likely to buy more cars, refrigerators and computers locally. While consumers may lose out a bit, consumer conglomerates such as Koc and Dogus could reap gains. Exporters are another beneficiary: Tourism has boomed this summer.

Consumers just can't do the same and buy local with oil and gas.

Because it doesn't have significant oil-and-gas resources, Turkey remains highly dependent on foreign energy. It imports around three-quarters of its total energy needs, according to the most recent International Energy Agency report, and energy makes up roughly two-thirds of the nation's current-account deficit.

If energy costs rise much more, they are likely to trigger a recession. Construction already is grinding to a halt. Ankara can cut fuel taxes to protect households and firms in the short term, but can't afford to take the hit indefinitely.

The only long-term solution is greater energy independence, which Turkish Finance Minister Berat Albayrak pledged to boost in last week's new economic program. But the Turkish government has made promises about hydroelectric and renewable sources for at least a decade, with little obvious effect.

The broader lesson is that a country's financial woes can be scary, but sometimes aren't the hardest problems to fix. Debts can be restructured and central banks can provide liquidity. Idle workers can be put to work through government programs: Turkey's public debt amounts to just 28% of GDP.

By contrast, when your currency tumbles, depending on others for essential goods has no easy way out.


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The Property Report
**Putnam Bets Big on Malls**

By Esther Fung
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Putnam Investments money manager Brett Kozlowski likes to buy bonds from government-sponsored enterprises Fannie Mae and Freddie Mac. But lately he has been boosting his funds' performance by wagering that some of the country's most downtrodden shopping malls will survive.

Mr. Kozlowski makes these bets by selling swaps related to a slice of an index known as the CMBX. His funds profit when prospects for weaker malls improve and they make their debt payments.

One of the mutual funds he manages, the Putnam Diversified Income Trust, had 14.6% of its $4.6 billion net assets invested in this CMBX trade as of the end of June, according to a Wall Street Journal analysis of fund filings. That is up from 10.6% of its net assets as of the end of September 2017.

The growing popularity of online purchases has devastated shopping malls across the U.S., forcing many stores to close and putting entire retail centers out of business.

But the pace of store closings this year has slowed. Tax cuts, low unemployment and gradually rising wages have prodded Americans to spend more, enabling some malls owners to open more stores.

This has made bets like Mr. Kozlowski's winners in 2018 after a dreadful 2017. The CMBX 6 has risen 3.8% so far this year, rebounding from a 9.5% loss last year, according to IHS Markit. Putnam reported that its Diversified Income Trust returned 2.5% over the first six months of the year.

The Putnam fund manager is no Luddite convinced that online shopping has peaked. Rather, Mr. Kozlowski said he believes that even if some stores falter, landlords can replace them with restaurants and entertainment or service-oriented tenants.

"I'm not counting on Macy's, J.C. Penney or Sears paying me my rent, it's just somebody needs to pay me my rent," said Mr. Kozlowski. "That's a big driver of how we think about this particular trade."

Consumers are still spending in areas where there is strong population and income growth, he added.

Mr. Kozlowski, 43 years old, was raised in upstate New York and joined Putnam in 2008. Some fund analysts worry that his fund's clients may not be fully aware that nearly 15% of the assets are betting on the survival of the weakest malls. This trade doesn't appear in the top-10-holdings section of the fund's annual and semiannual reports.

While the fund has reported strong returns in the last three years, it has been **volatile**, said Todd Rosenbluth, senior director of ETF and mutual-fund research at CFRA. During much of last year, the shopping-mall trade weighed on returns and increased **volatility**.

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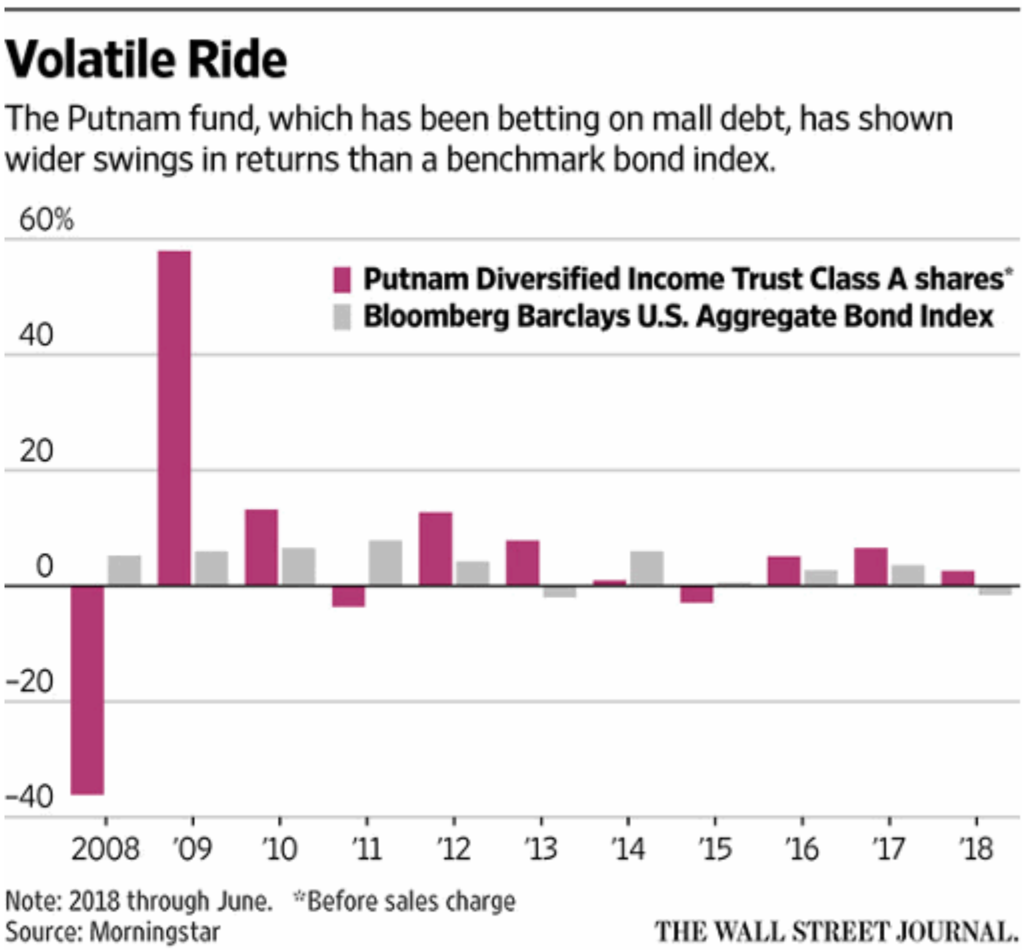
AllianceBernstein LP, another company taking a **bullish** position, said that while 10 malls out of the roughly 40 malls reflected in the index are likely to become obsolete, the majority of the malls are still able to secure reasonable leasing terms.

Putnam began raising its bets in the derivative early last year, when the index declined. At the lower price, Putnam determined that the index offers better liquidity and value compared with the bonds.

"There are underlying names that we don't like that could potentially take losses, but you're getting compensated for that by the price," said Mr. Kozlowski.

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The New York Times

STOCKS & BONDS
Business/Financial Desk; SECTB

**Rising Oil Prices and Interest Rates Weigh on the Market**

By THE ASSOCIATED PRESS
933 words
26 September 2018
The New York Times
NYTF
Late Edition - Final
2
English


Major U.S. indexes finished mostly lower Tuesday as rising interest rates hurt stocks that pay big dividends and higher **oil prices** pushed transportation and shipping companies lower. The **S&P 500 index** fell for the third day in a row.

**Oil prices** continued to rise after a weekend meeting of OPEC and its allies ended without an increase in oil production. That's helped energy companies, but it is pressuring airlines and other companies that will have to pay more for fuel. Higher **oil prices** can also ripple through the economy and increase inflation, and that's helped push interest rates higher this week.

On Wednesday the Federal Reserve is expected to increase its benchmark interest rate for the third time this year. Investors have been sure for months that the Fed would raise rates at this meeting, so they'll be focusing on the Fed's economic projections and Chairman Jay Powell's press conference afterward.

"He'll want to say as little as possible about tariffs, about fiscal policy, and say as little as possible about any advice the president may be giving him and the Federal Reserve about how to run monetary policy," said David Kelly, chief global strategist for JPMorgan Funds. But Kelly said the reporters will likely probe Powell's views on all of those topics.

The **S&P 500** fell 3.81 points, or 0.1 percent, to 2,915.56. The **Dow Jones Industrial Average** lost 69.84 points, or 0.3 percent, to 26,492.21. The **Nasdaq composite** added 14.22 points, or 0.2 percent, to 8,007.47. The Russell 2000 index of smaller-company stocks gained 3.49 points, or 0.2 percent, to 1,708.80.

**Bond prices** kept falling as the Fed meeting began, sending yields higher. The yield on the **10**-**year Treasury** note rose to 3.10 percent from 3.07 percent a day earlier.

Rising bond yields tend to hurt high-dividend companies, which many income-seeking investors see as substitutes for bonds. Among utilities, Southern Co. fell 2.5 percent to $42.73 and consumer goods maker Procter & Gamble lost 1.4 percent to $83.12.

Stocks usually do well when the Fed starts to raise interest rates because the higher rates reflect solid economic growth, which is associated with strong company profits. But as the rate increases continue, in line with the Fed's goal of keeping inflation in check, the effect on stocks can become negative as economic growth slows.

**Oil prices** have climbed recently because OPEC isn't producing more oil, while Iran is exporting less after the U.S. withdrew from the international nuclear deal with Iran and announced more sanctions on the country.

Benchmark U.S. crude rose 0.3 percent to $72.28 a barrel in New York. Brent crude, the standard for international **oil prices**, rose 0.8 percent to $81.87 a barrel in London. Brent crude is at its highest price since November 2014.

ConocoPhillips rose 1.4 percent to $78.11 and Philips 66 added 1.3 percent to $114.88.

Drive-in restaurant chain Sonic jumped 18.7 percent to $43.46 after it agreed to be bought by Inspire Brands, which also owns Arby's and Buffalo Wild Wings. The purchase values Sonic at $43.50 a share, or $1.57 billion. Inspire Brands is controlled by the private equity firm Roark Capital.

XO Group, which runs the wedding marketplace The Knot, jumped 26.3 percent to $34.91 after it accepted a $907 million offer from two funds that own its competitor WeddingWire.

Companies around the world have announced $3.26 trillion in deals this year, according to Dealogic, far above the $2.49 billion in deals that were struck over the first three quarters of 2017. The recent U.S. corporate tax cut and low interest rates have contributed to that trend.

If the Fed does raise interest rates Wednesday, it would be the ninth increase since late 2015 and would take the benchmark rate to a range of 2 percent to 2.25 percent, with another increase expected this year and more to come in 2019.

Wholesale gasoline added 0.6 percent to $2.07 gallon. Heating oil rose 0.8 percent to $2.31 a gallon. Natural gas rose 1.4 percent to $3.08 per 1,000 cubic feet.

Gold rose 0.1 percent to $1,205.10 an ounce. Silver gained 1.1 percent to $14.49 an ounce. Copper fell 0.4 percent to $2.82 a pound.

The dollar rose to 112.93 yen from 112.73 yen. The euro rose to $1.1767 from $1.1758.

The British FTSE 100 index rose 0.7 percent. The DAX in Germany added 0.2 percent and France's CAC 40 gained 0.1 percent.

Tokyo's Nikkei 225 gained 0.3 percent and the Sensex in India slipped 0.1 percent. Markets in Hong Kong and Seoul were closed for holidays.

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AP Markets Writer Marley Jay can be reached at http://twitter.com/MarleyJayAP His work can be found at https://apnews.com/search/marley%20jay

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); Consumer Confidence: Index measures attitudes toward the economy, 1985 = 100. (Source: The Conference Board)

Document NYTF000020180926ee9q0005e

 

THE WALL STREET JOURNAL.
U.S. EDITION

**The Fault Lies in R-Star and in Ourselves**

By Kevin Warsh
954 words
26 September 2018
The Wall Street Journal
J
A17
English


The American financial system was at grave risk of collapse in September 2008. It was among the darkest economic periods in our nation's history. All of us who were then on the front lines at the Federal Reserve and the Treasury have since repaired to less strenuous confines.

The lens of time gives us a clearer, more complete picture of events. Many are using this 10-year anniversary to debate the wisdom of particular responses to the crisis. But we should also convey to our successors which policy ideas now in fashion should be reconsidered or discarded.

Before the onset of the 2008 crash, for example, price stability was thought to be a fair proxy for financial stability. Stable growth and steady, moderate inflation were thought to be persistent features of the macroeconomy. Central-bank announcements were to be aimed at dampening natural market **volatility**. Some still believe such things, despite strong evidence to the contrary.

Today, the idea most in vogue in central-bank circles is something called "r-star" -- the neutral real interest rate at which monetary policy is neither accommodative nor restrictive. Many policy makers and academics now recommend setting Fed interest rates principally by determining r-star. But like many great theoretical insights -- this one originally offered by Swedish economist Knut Wicksell in 1898 -- r-star has been pushed well beyond its practical utility.

Policy makers are currently rejoicing in their good fortune. The U.S. economy is booming: Output is growing more than 50% faster than the Fed forecast a year ago, wages are accelerating, and labor markets are the strongest they've been in at least a generation. Capital investment is strengthening, and productivity shows some improvement. Asset prices are high. Credit is cheap and widely available. And inflation is running at or near the Fed's avowed target.

The Trump administration's reforms in tax and regulatory policy were well-timed. They caused a business and wage-earner expansion to follow on the heels of a consumer-driven, housing-led expansion that was starting to show its age. The strong trends in the U.S. economy are likely to continue.

Even so, history and hard experience tell us that a boom is not a time for triumphalism, especially for the guardians of financial stability at the Fed. The most consequential period in economic policy is often when the embers of the last fire are gone and the first sparks of the next are not yet visible. Policy makers should not be dismissive of less likely, but more damaging tail events.

There are risks on the horizon. An escalating trade war between the world's two largest economic powers is happening in real time, though a detente could still be reached. Weaknesses across emerging markets are growing, but lenders and counterparties might escape unscathed. The biggest banks just passed their "stress tests" with flying colors -- meaning either that they are insulated from failure or that the tests have lost probative value. The "term premium," which affects long-term funding costs for debtors, is near its lowest level in a half-century. It might stay there for a while, but risks are often highest when market measures are lowest.

Are discussions of these risks central to the Fed's pending policy decision? Not according to recent Fed statements, speeches and meeting minutes, which suggest the predominant policy focus is r-star.

In my view, r-star is not a beacon in the sky but a chimera in the eye. The idea of a "neutral" rate is a useful fiction. It makes for an interesting academic thought experiment. In practice, though, it's unobservable, unpredictable, imprecise and highly variable. That makes it a poor guide for policy makers.

The Fed's search for the neutral rate suffers significant failings. First, productivity growth should be a big factor in determining the neutral rate, but productivity forecasts have been wildly off the mark for the past couple of decades.

Second, the neutral rate is endogenous to economic policy. Policy makers' own choices about taxes, spending, regulation and trade alter the economy's potential growth in lagged and imprecise ways and thus affect any meaningful estimate of r-star.

Third, monetary policy today is not just about rates. The Fed's balance sheet, including nearly $3 trillion of excess assets owing to crisis-inspired quantitative easing, makes monetary policy considerably looser. If the Fed's balance sheet isn't neutral, a neutral interest rate is all the more difficult to ascertain. Unwinding quantitative easing before rate hikes would have been far preferable as a policy matter.

Finally, the search for a neutral rate is significantly affected not only by the Fed, but also by the monetary policy choices of other large central banks. The Fed's domestic, closed-economy bias adds even more obstacles to an already overambitious adventure in policy-making.

Reducing the conduct of monetary policy to a star, or a rule, is tempting but unwise. In his recent remarks at Jackson Hole, Wyo., Fed Chairman Jerome Powell showed suitable humility in questioning the location of r-star. He should go further and question the whole notion that r-star has any significant practical use for the Fed. Rarely are complex problems solved by pointing to a single, hard-to-reach object and assigning magical properties to it. As Shakespeare's Julius Caesar reminds us: "The fault, dear Brutus, lies not in the stars but in ourselves."

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Mr. Warsh, a former member of the Federal Reserve Board, is a distinguished visiting fellow in economics at Stanford University's Hoover Institution.



Document J000000020180926ee9q0000l

THE WALL STREET JOURNAL.

Markets

**Health-Care Stocks Lead This Leg of Rally, After Tech Giants' Stumbles; Hedge funds and money managers have been building up positions in health-care stocks as a safety play for an eventual slowdown**

By Michael Wursthorn
1,015 words
25 September 2018
05:10 PM
The Wall Street Journal Online
WSJO
English


Health-care stocks have emerged as market leaders in the third quarter, helping push major U.S. indexes to new highs.

One reason: Money managers are embracing the sector as a safety play, particularly after big technology stocks stumbled in September.

The **S&P 500**'s health-care sector is the best performer of the index's 11 groups in the third quarter, up 13% and on pace for its strongest showing in more than five years. On a year-to-date basis, health-care stocks are trailing only the technology and consumer-discretionary sectors.

Hedge funds have built up their biggest position in health-care shares of the past five years. About 17% of their assets are in the sector, second only to shares of tech companies, according to Goldman Sachs Group Inc. data through June. Mutual-fund managers have also been shifting into health-care stocks, with many building outsize positions, according to Goldman's data.

And flows into health-care-focused mutual funds and exchange-traded funds, which are popular with retail investors, are at their strongest in three years, according to Morningstar Inc.

Rising interest in the stocks coincides with surging profits across the industry. Plus, the health-care needs of an aging population are expected to insulate the companies from a downturn, and investors searching for attractively valued stocks after a nine-year **bull market** in the U.S. have embraced the shares.

The sector's rally has been broad, with shares of pharmaceutical giants like Merck & Co. and Pfizer Inc., insurers including Humana Inc. and UnitedHealth Group Inc., and equipment suppliers like Abiomed Inc. and Align Technology Inc. all rising at least 20% in 2018.

"These stocks had been out of favor for a while," said Tom Hancock, head of focused equity at Grantham, Mayo, Van Otterloo & Co., the Boston-based money-management firm founded by famed investor Jeremy Grantham.

"But we've been trying to find stocks that aren't being inflated by this rising tide of economic good news," Mr. Hancock added, referring to the strong U.S. growth that has helped fuel a broad **stock-market** upswing in recent years. "When that tide recedes, we're looking for companies that will be OK in that environment."

Big tech stocks that have led much of this year's rally, including Amazon.com Inc., Google parent Alphabet Inc. and Apple Inc., which each fell more than 3% in September. Investors have cut their exposure amid concerns about new regulations in the wake of Facebook Inc.'s data mishap.

At firms like GMO, investors have been trimming their technology holdings to help fund their shifts into health care. GMO's funds recently initiated a position in Merck, Mr. Hancock said, as the pharmaceutical giant has focused on further developing cancer-treatment drug Keytruda, which accounted for about 9% of the company's total revenue last year. Merck shares have surged 26% this year and 16% in the third quarter alone.

GMO funds, meanwhile, trimmed stakes in Alibaba Group Holding Ltd. and Microsoft Corp. in the past six months, according to FactSet.

Similarly, hedge-fund manager Tudor Investment Corp. increased its stake in health insurer Aetna Inc. and initiated new positions in drugmakers Shire PLC and AbbVie Inc. all in the last six months, according to fund-holdings data compiled by FactSet. Millennium Management LLC, another hedge fund, added to its positions in medical-device makers Medtronic PLC and Boston Scientific Corp.

Tudor declined to comment through a spokesman. Millennium didn't respond to a request for comment.

Some investors, though, question the timing of health care's sudden appeal, citing its bouts of **volatility** when political debates over how Americans pay for health care intensify. The sector will likely see another jolt should Republicans retain control of Congress in November's midterm elections and resume talks of a health-care overhaul, said Lewis Piantedosi, a vice president and portfolio manager for Eaton Vance Management, which has kept its allocation toward health-care stocks below its benchmark.

Still, the broader shift into health-care stocks suggests investors are eschewing risk after a long rally. Although the tax cut enacted in December led to an explosion in corporate profits that fueled the latest leg of the rally, Wall Street analysts and economists are increasingly convinced that the U.S. economy will start contracting as early as 2020.

Investors tend to view health-care stocks as a defensive investment because health insurers, pharmaceutical companies and medical-device makers usually hold up better in times of economic turbulence. That is because most medical expenses can't be put off in a recession, and economic swings don't typically curb the rollout of new drugs and devices. Valuations are also enticing, investors said, with health-care stocks in the **S&P 500** trading in line with the broader **S&P 500** at about 17 times future earnings, compared with 18 times for the tech sector and 23 times for consumer-discretionary companies, according to FactSet.

Biotech firms, however, are viewed as riskier and aren't getting nearly as much attention from big money managers, some investors said, because those stocks can move dramatically based on drug approvals. Biotech shares in the **S&P 500** aren't seeing the same bump as pharmaceutical giants, insurers and medical suppliers.

"Not to say it can't continue, but we're in the longest **bull market** ever," said Matthew Watson, a portfolio manager and assistant vice president at James Advantage Funds, a mutual-fund manager that has boosted its positions in health-insurer Anthem Inc. and drugmaker Pfizer. "So from a risk standpoint, getting into health-care stocks, which tends to be defensive, makes sense for us too."

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

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U.S. Markets
Markets
**U.S. Stocks Tick Higher as Oil, Energy Stocks Extend Gains; President Trump and his South Korean counterpart Moon Jae-in signed a renegotiated free-trade agreement at the U.N.**

By Michael Wursthorn
669 words
25 September 2018
04:31 PM
The Wall Street Journal Online
WSJO
English


* Oil and energy stocks extend gains

* Traders absorb China's exit from talks

* Investors eye Fed meeting

The **S&P 500** edged lower on Tuesday, as interest-rate sensitive stocks sold off late in the session and offset gains among shares of oil-and-gas companies.

The corners of the **stock market** sensitive to rising interest rates were among the worst performers ahead of Wednesday's Federal Reserve meeting. Utility stocks, which are viewed as a bond proxy because of the relatively high dividends they pay, sank 1.2% in the **S&P 500**—more than any other industry group.

Shares of consumer staples and financial stocks, both of which also tend to move based on interest-rate expectations, slid in afternoon trading as well. Those losses offset another strong day for energy stocks, which have rallied 10 of the past 11 trading days. The sector's latest leg of gains followed the Organization of the Petroleum Exporting Countries' decision to stick to current production quotas.

The Fed is largely expected to raise interest rates Wednesday and again in December for a total of four increases this year. Rising rates tend to reduce appetite for high-yielding, less risky stocks as investors can find better premiums in other asset classes, such as bonds.

But the real focus is likely to be on any clues as to how the central bank plans to proceed with next year's pace of increases as well as its view of the U.S. economy, especially with the continuing trade dispute still running in the background.

"With a rate hike all but priced in, markets will be focused on the policy path in 2019 and any sign of changes in inflation expectations," said John Lynch, chief investment strategist for brokerage firm LPL Financial. "Any change in the Fed's view of inflation could roil markets," Mr. Lynch said, adding upbeat U.S. economic data should keep the Fed on course for now.

The **S&P 500** slid 0.1% to notch its third consecutive decline, while the **Dow Jones Industrial Average** shed about 70 points, or 0.3%, to 26492. The **Nasdaq Composite**, meanwhile, rose 0.2%.

The **S&P 500**'s minor move extended the broad index's run without a 1% move up or down to 64 trading sessions, back to late June. The pullback in big market swings coincides with investors' nervousness around the continuing trade dispute, the Fed's rate-hike path beyond this year and the fact that the nine-and-a-half-year **stock-market** rally is the longest ever.

Trading saw nearly all the utility stocks in the **S&P 500** fall, with electricity provider Southern down 2.3%, putting it among the sector's worst performers.

Bank and other financial stocks in the broad index declined 0.4%, while consumer staples, which also tend to pay relatively big dividends, fell 0.7%.

Semiconductor stocks also weighed on major indexes. The industry, already bruising from the trade fight, got another dose of bad news after a Raymond James analyst lowered his rating on shares of Intel to underperform from market perform, citing delays in chip production, and cut his outlook on several rivals.

Intel's stock fell 2.1%, while the PHLX Semiconductor Index, which tracks the shares of 30 chip makers, slumped 1.7%.

Energy company Concho Resources, meanwhile, rose 2.6%, putting it among the **S&P 500**'s biggest gainers, while oil-field services business Baker Hughes added 1.9%.

The energy sector has been getting a late-quarter boost from a rally in **oil prices** that sent the commodity soaring toward its highest close in nearly four years.

David Hodari contributed to this article

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

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THE WALL STREET JOURNAL.

Markets

**Putnam Bond-Fund Manager Bets Big on Depressed Malls; Brett Kozlowski boosts performance by wagering that some of the most downtrodden shopping malls will survive**

By Esther Fung
837 words
25 September 2018
07:00 AM
The Wall Street Journal Online
WSJO
English


Putnam Investments money manager Brett Kozlowski likes to buy bonds from government-sponsored enterprises Fannie Mae and Freddie Mac. But lately he has been boosting his funds' performance by wagering that some of the country's most downtrodden shopping malls will survive.

Mr. Kozlowski makes these bets by selling swaps related to a slice of an index known as the CMBX. His funds profit when prospects for weaker malls improve and they make their debt payments.

One of the mutual funds he manages, the Putnam Diversified Income Trust, had 14.6% of its $4.6 billion net assets invested in this CMBX trade as of the end of June, according to a Wall Street Journal analysis of fund filings. That is up from 10.6% of its net assets as of the end of September 2017.

The growing popularity of online purchases has devastated shopping malls across the U.S., forcing many stores to close and putting entire retail centers out of business.

But the pace of store closings this year has slowed. Tax cuts, low unemployment and gradually rising wages have prodded Americans to spend more, enabling some malls owners to open more stores.

This has made bets like Mr. Kozlowski's winners in 2018 after a dreadful 2017. The CMBX 6 has risen 3.8% so far this year, rebounding from a 9.5% loss last year, according to IHS Markit. Putnam reported that its Diversified Income Trust returned 2.5% over the first six months of the year.

The Putnam fund manager is no Luddite convinced that online shopping has peaked. Rather, Mr. Kozlowski said he believes that even if some stores falter, landlords can replace them with restaurants and entertainment or service-oriented tenants.

"I'm not counting on Macy's, J.C. Penney or Sears paying me my rent, it's just somebody needs to pay me my rent," said Mr. Kozlowski. "That's a big driver of how we think about this particular trade."

Consumers are still spending in areas where there is strong population and income growth, he added.

Mr. Kozlowski, 43 years-old, was raised in upstate New York and got to know some of the local malls, shopping at Finger Lakes Mall in Auburn, N.Y., and Destiny USA mall in Syracuse. After receiving an economics degree at the Massachusetts Institute of Technology and working at Fidelity Investments for more than a decade, he joined Putnam in 2008. He noted that his family shops online and at the nearby Natick Mall.

Some fund analysts worry that his fund's clients may not be fully aware that nearly 15% of the assets are betting on the survival of the weakest malls. This trade doesn't appear in the top-10-holdings section of the fund's annual and semiannual reports.

While the fund has reported strong returns in the last three years, it has been **volatile**, said Todd Rosenbluth, senior director of ETF and mutual-fund research at CFRA. During much of last year, the shopping-mall trade weighed on returns and increased **volatility**.

"If a fund is investing in a less liquid security, that is a risk that investors should be cognizant of," he said.

Putnam says it has fully complied with regulatory standards on disclosure.

AllianceBernstein LP, another company taking a **bullish** position, said that while 10 malls out of the roughly 40 malls reflected in the index are likely to become obsolete, the majority of the malls are still able to secure reasonable leasing terms.

The shopping-mall bet is not the first time that the Putnam Diversified Income Trust fund took on unconventional risks to boost its returns. Morningstar Inc. said the fund has a history of taking on high levels of debt and investing in derivatives such as collateralized mortgage obligations and mortgage-backed bonds, which hurt its performance during the 2008 financial crisis. Morningstar said the fund also had 'flashes of brilliance' when the market rebounded in 2009 and 2010.

Mr. Kozlowski didn't manage the fund during these periods, but since 2010 he has played a role as a commercial-mortgage analyst.

Putnam began raising its bets in the derivative early last year, when the index declined after New York-based hedge-fund manager Eric Yip first circulated a report that mapped out a dire outlook for some malls.

At the lower price, Putnam determined that the index offers better liquidity and value compared with the bonds.

"There are underlying names that we don't like that could potentially take losses, but you're getting compensated for that by the price," said Mr. Kozlowski.

Write to Esther Fung at esther.fung@wsj.com

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THE WALL STREET JOURNAL.

Business
**BMW Cuts Outlook, Blames Trade Disputes and Emissions Costs; New emissions standards and the U.S.-China trade dispute are weighing on the luxury car maker**

By William Boston
602 words
25 September 2018
10:30 AM
The Wall Street Journal Online
WSJO
English


BERLIN—Shares in BMW AG fell by as much as 6% on Tuesday after the luxury car maker warned that emissions-related costs, product recalls and fierce price competition amid global trade disputes would dampen profit this year.

BMW said the main reason for the dimmer outlook was the cost of adjusting to new global rules for emissions testing to measure pollutants, greenhouse gas emissions, and fuel economy. The test, called world harmonized light vehicles test procedure, or WLTP, came into force in Europe in September and BMW racked up significant costs earlier in the year to adapt its vehicles to the new regime.

The profit warning comes amid a flurry of similar concerns from other companies in the sector, such as rival Daimler AG and supplier Continental AG, which have spoken out against disruptions to global markets and supply chains from political tensions and the U.S.-China trade dispute.

Several industry analysts saw BMW's unexpected warning as a turning point in the industry, a sign that regulatory challenges and a **volatile** global trade environment would further hit sales and dent corporate profits. Analysts had expected weak auto industry performance in the three months to October to improve at the end of the year, but now fear it will continue.

"Today's warning has extinguished the idea that the sector will rally again after a well-flagged soft third-quarter," said Patrick Hummel, an automotive analyst at UBS.

Analysts cut their earnings outlook for BMW by about €1.2 billion ($1.4 billion), bringing consensus estimates down to about €9.7 billion.

When BMW set its original guidance for 2018 earlier this year, it said it expected a challenging year on account of around €1 billion in upfront costs to develop new technology and currency headwinds in the "mid-to-high three-digit million euro range."

That assessment now looks optimistic.

The company now said it anticipated full-year pre-tax profit for the entire company "to show a moderate decrease" from the previous year and revenue from its automotive businesses to be "slightly lower."

BMW had previously forecast a slight increase in automotive revenue and pretax earnings at about the same level as last year. In 2017, it reported pretax earnings of €10.7 billion and automotive revenue of €88.6 billion.

The Munich-based car maker also lowered the guidance on its profit margin in the automotive segment to "at least 7%" from a previous estimate of a range of 8% to 10%.

The company also cited increased goodwill and warranty costs associated with product recalls and the impact of price reductions on vehicles sold in China in the wake of the continuing trade dispute between the U.S. and China. However, BMW declined to quantify the full financial impact of these issues.

The warning sent the company's shares down 5.7% to €78.75 in midafternoon trading in Frankfurt. They later recovered to €80.35, down 4%.

All major European auto makers gave up today's gains in the wake of BMW's profit warning. The biggest loser was Peugeot SA, which fell 2.5% after the news, while Fiat Chrysler Automobiles NV was least hit, falling 0.5%.

Write to William Boston at william.boston@wsj.com

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The New York Times

Fact Check of the Day
World
**Fact-Checking Trump's Speech to the United Nations**

By Linda Qiu
1,025 words
25 September 2018
07:11 PM
NYTimes.com Feed
NYTFEED
English


Mr. Trump rattled off a list of accomplishments on the economy, tax cuts, military spending and the border — many of them cherry-picked, exaggerated or false.

He is right that the United States **stock market** is soaring, and unemployment rates for Hispanics, African-Americans and Asian-Americans have reached record lows.

But he omitted less flattering indicators when describing an economy "booming like never before." For example, G.D.P. growth is healthy, but reached higher points as recently as 2014. The unemployment rate is at an 18-year low, but is higher than several months during the 1940s and 1960s. And wage growth is still slow: after adjusting for inflation, average hourly earnings increased just 0.2 percent in August.

Mr. Trump's claim of signing the "biggest" tax cut in American history is false; by various metrics, several rank higher. He misleadingly said construction on the border wall with Mexico had begun; projects to replace fencing and barriers are underway, but the administration has not begun to build a 1,000-mile-long wall. He was also wrong in characterizing recent military spending bills as "record funding." Even without adjusting for inflation, President Barack Obama signed legislation in 2010 that provided more money for the military.

Additionally, Mr. Trump has signed a relatively low number of bills when compared to other presidents, even at similar points in their terms. While he can claim major legislative victories — on tax cuts and veterans' benefits — he has also been unable to deliver on other key campaign promises, like the border wall and repealing and replacing the Affordable Care Act.

Mr. Trump's declaration of victory is slightly premature. The Islamic State is down to its last 200 square miles, about 1 percent of the territory it previously held in Iraq and Syria, The New York Times recently reported. Pentagon officials have stressed that their job is not done.

There are still "remaining pockets" of Islamic State fighters in Syria and Iraq, and they continue to threaten the two countries' peace and security, Col. Sean J. Ryan, a Defense Department spokesman, told reporters on Sept. 18.

Defense Secretary Jim Mattistold reporters on Monday that American troops will continue to train and advise local security forces to make certain the Islamic State does not resurface. He said "fighting is ongoing" in Syria's Euphrates River Valley, where troops have been battling the Islamic State.

"I think that getting rid of the caliphate doesn't mean you then blindly say 'O.K., we got rid of it,' march out, and then wonder why the caliphate comes back,' Mr. Mattis said. "And how many times have we seen — look at even Iraq where they're still on the hunt for them. And they're still trying to come back."

Mr. Trump is right that the United Arab Emirates, Saudi Arabia and Qatar have contributed funds to ease humanitarian crises in Syria and Yemen. But his comment glosses over the three countries' roles in Yemen's civil war.

The governments of Saudi Arabia and the U.A.E. are the top two donors to the United Nations' humanitarian response plan in Yemen, contributing nearly $1 billion combined. Additionally, the two countries donated an additional $375 million through other programs, the data show. Qatar also contributed $500,000 to the United Nations response plan.

In Syria, Saudi Arabia donated $18.6 million this year to the world body's humanitarian response plan and $24.3 million in 2017. Qatar contributed $2.2 million in 2018 and $29.5 million last year, the same reports show.

Dollars aside, it's worth noting that the United Nations and human rightsgroups have said that the humanitarian crisis in Yemen has been exacerbated by the country's continuing civil war. A Saudi-led coalition — including the U.A.E. and the United States — has since 2015 fought Iranian-linked Houthi rebels who ousted the government of President Abdu Rabbu Mansour Hadi of Yemen.

Qatar initially was part of the international coalition fighting the Houthi rebels, but was expelled last year after Riyadh accused the tiny nation of funding terrorism, cozying up to Iran and welcoming dissidents.

A report by United Nations investigators in August accused the Saudi-led coalition of potential war crimes, including charges of killing thousands of civilians in airstrikes, torturing detainees and conscripting child soldiers. The same report also accused the Houthi rebels of possible war crimes.

The reaction to the United States' withdrawing from the Iran nuclear deal in May was more varied in Middle Eastern countries than Mr. Trump's claim would suggest.

Saudi Arabia, the U.A.E., Bahrain and Israel issued statements supporting Mr. Trump's decision.

But Syria, Iraq and Lebanon voiced disappointment. Jordan's foreign minister warned of a potential arms race in the region absent the nuclear deal. Qatar, Egypt, Kuwait and Oman issued cautious statements that stressed their commitments to peace in the Middle East, but did not take clear positions on the United States' withdrawal.

Outside of the Middle East, global reaction toward Mr. Trump's decision has largely been negative. The six other parties to the treaty with Iran — Britain, France, Germany, China, Russia and the European Union — opposed the withdrawal. So did Canada, Australia, Ireland, Japan, Norway, the Netherlands, South Africa and Sweden, according to statements compiled by the Arms Control Association.

As The New York Times and others have repeatedly reported, Mr. Trump is overstating the figure by about $250 billion. Last year, the United States had an overall trade deficit of $552 billion, according to the Census Bureau. That included a goods deficit of $807 billion, offset by a trade surplus in services of $255 billion.

Mr. Trump's preoccupation with trade in goods contradicts his own White House economic report, which he signed and was released in February.

The American economy has shifted "away from manufacturing and toward service provision industries" in recent decades, according to the report. "Focusing only on the trade in goods alone ignores the United States' comparative advantage in services."

Document NYTFEED020180925ee9p009yd

 

THE WALL STREET JOURNAL.

Markets
**Copper Stalls as Markets Awaits Fresh Trade Signals**

By David Hodari and Amrith Ramkumar
417 words
25 September 2018
10:12 AM
The Wall Street Journal Online
WSJO
English


Copper prices swung between small gains and losses on Tuesday, with traders looking ahead to the next trade updates from the U.S. and China.

Copper for December delivery was recently up 0.1% at $2.8390 a pound on the Comex division of the New York Mercantile Exchange. Prices have rebounded lately after entering **bear-market** territory this summer, though they are still well below their June four-year highs amid worries that a tariff fight between the U.S. and China will weaken the global economy and limit consumption.

China is the world's largest consumer of industrial metals broadly, accounting for about half of global copper demand.

Although the U.S. and China have laid out plans to end their tariff fight ahead of planned November meetings between leaders from both countries, the latest duties from both sides took effect on Monday.

China also canceled trade talks that were planned for this week.

Analysts are also keeping an eye on the dollar, which has fallen lately after hitting a 15-month high last month. A weaker dollar makes commodities cheaper for overseas buyers and has helped materials stabilize following punishing drops in the summer. The WSJ Dollar Index, which tracks the dollar against a basket of 16 other currencies, was down 0.1% Tuesday.

Among precious metals, gold for December delivery added 0.2% to $1,206.80 a troy ounce. Prices have fallen about 8% this year, hurt by the dollar's stability and higher short-term Treasury yields that have made gold less attractive to some investors. Traders were looking ahead to Wednesday's statement from the Federal Reserve for the latest reading on the central bank's plan for interest-rate increases.

Elsewhere in precious metals, most-actively traded silver futures rose 1.1% to $14.495 a troy ounce. Platinum was down 0.3% at $827.30, while palladium climbed 0.6% to $1,058 in a 10th straight session of gains.

On the London Metal Exchange, aluminum for delivery in three months inched up 0.4% to $2,067.50 a metric ton. Zinc dropped 0.7% to $2,545.50, tin was down 0.1% at $18,900 and nickel edged up 0.2% to $12,975. Lead fell 0.4% to $2,035.

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Document WSJO000020180925ee9p0030d

WSJ PRO CENTRAL BANKING

Economy
**BOJ to Weigh Merits, Demerits of Easing in 'Balanced Manner,' Kuroda Says; Japanese central bank to maintain rate targets for "a fairly long period of time"**

By Megumi Fujikawa
461 words
25 September 2018
05:31 AM
WSJ Pro Central Banking
RSTPROCB
English


OSAKA—Bank of Japan Gov. Haruhiko Kuroda said the central bank is paying attention to both the merits and demerits of monetary easing, but that doesn't mean it has given up on its 2% inflation target.

The Japanese economy is on a recovery path, but price and wage growth remain sluggish after more than a decade of deflation. Under such circumstances, the Japanese central bank needs to keep an eye on the positive and negative effects of its easing policy "in a balanced manner," Mr. Kuroda said Tuesday in a speech to business leaders in Osaka.

"We will come up with measures to support market and banking functions if necessary. But we will do so to continue easing, not to deny it," he said at a news conference later in the day. He added that possible side effects of easing won't deter the bank from taking additional action if necessary.

His comments came after a number of policy tweaks the bank made in July confused investors over the direction it is heading amid the global wave of monetary tightening.

Mr. Kuroda said forward guidance introduced in July means that the bank will maintain short- and long-term rate targets for "a fairly long period of time." While the forward guidance wasn't based on any specific period, it doesn't mean ultralow rates would continue indefinitely, he added.

The central bank stood pat on policy last week after making a number of tweaks in July to prepare for a longer-than-expected fight to lift inflation, which has yet to reach the bank's target.

Mr. Kuroda said Tuesday that allowing the 10-year Japanese government-**bond yield** to move in a wider range will mitigate the side effects of easing, including low market **volatility**, and facilitate the formation of an appropriate yield curve.

It will eventually lead to "sustainability of the policy," he said.

On the economic outlook, Mr. Kuroda pointed out some uncertainties, including the trade spat between the U.S. and China.

"Careful attention should be paid to a risk that the impact might increase through market instability or corporate sentiment," he said, responding to an audience member's question. Osaka is headquarters to exporters ranging from electronics to machinery makers.

The bank will also monitor the effects of monetary-policy normalization by some central banks, including the Federal Reserve, on global capital flows and emerging economies, Mr. Kuroda said, adding, however, that it is "fairly unlikely" to cause any serious problem to the global economy at this point.

Write to Megumi Fujikawa at megumi.fujikawa@wsj.com

Document RSTPROCB20180925ee9p0002t

THE WALL STREET JOURNAL.
U.S. EDITION

**U.S. News: Disneyland's Hometown Relations Sour --- City of Anaheim spars with company over tax breaks valued at hundreds of millions**

By Nour Malas
1,105 words
25 September 2018
The Wall Street Journal
J
A3
English


ANAHEIM, Calif. -- Six decades after Walt Disney built his first theme park here on a plot of orange groves, Disneyland and the city it calls home are at each other's throats.

Tapping public animus toward corporate subsidies, Anaheim politicians are questioning the wisdom of granting Walt Disney Co. hundreds of millions of dollars in tax breaks to support expansion. The city terminated the largest of those deals last month.

The issue is resonating with some residents who wonder why a theme park that can't move, owned by a conglomerate worth some $166 billion, needs financial incentives at a time of rising costs for residents and city governments in California.

"It's as if somehow we should feel fortunate that Walt Disney chose Anaheim," said city council member Jose Moreno, who was elected in 2016 as part of what locals call the first "anti-Disney" majority. "Maybe we should, but they should be grateful for a city that has helped them grow."

While many American cities are desperate to draw major corporate employers, others are grappling with the costs of hosting them. Debates similar to the one in Anaheim have flared up in Seattle, home to Amazon.com Inc., and over Alphabet Inc.'s Google and Apple Inc. in Silicon Valley.

The tipping point in Anaheim came after the city attorney told Disney in August that its decision to move a planned luxury hotel's location by 1,000 feet disqualified it from a previously approved 20-year, $267 million tax rebate. Disney saw the relocation as a technicality, but the city council wouldn't renegotiate, so the company suspended construction.

Rather than keep fighting, Disney tried to quell the political hostility by asking the city to end two major incentive deals because they had become "a flashpoint for controversy and dissension in our community," Disneyland Resort President Josh D'Amaro wrote in a letter to the city. Anaheim officials voted to terminate both subsidies a week later on Aug. 28.

Still, Disneyland executives warn that tax deals were critical to the resort's multibillion-dollar expansions this century and that the recent political **volatility** puts future investment at risk.

"The evolving environment in Anaheim makes it difficult for us to set and execute long-term strategies," Mr. D'Amaro said in a statement. "We will always invest in the Disneyland Resort, but what's at stake now is the level of that investment, particularly relative to other cities where the business climate is more stable."

Disneyland, which opened in 1955, drew nearly 28 million visitors last year and employs 30,000 people. Hotel tax revenue, driven largely by Disney visitors, more than tripled in the past 20 years to $155.6 million and accounts for nearly half of the city's general fund.

Tom Daly, who was Anaheim's mayor at the time of a key 1996 financing agreement with Disney, said mutual investments transformed the city into a global tourist destination. The city's current leadership, he said, "inherited very healthy revenues, and now they are critiquing the source of those revenues."

Despite the end of its tax subsidies, Disney remains a source of political tension in this city of 350,000. Anaheim voters this fall will decide on a new mayor, three city council seats, and a minimum-wage increase for big hospitality businesses in an election centered on the media giant.

Mayoral candidate Ashleigh Aitken, a consumer-protection attorney, is largely focusing her campaign on opposition to corporate subsidies.

"Like most Anaheim residents, I love Disneyland. And I, like most of Anaheim, got fed up of being taken for a ride outside of the park," Ms. Aitken said.

Disney has spent hundreds of thousands of dollars each election year in the past decade to back friendly candidates. City leaders said collaborating with the company was rarely controversial until 2015, when the city council agreed to extend a longstanding agreement to protect Disney from ticket taxes. The company, in turn, committed to build a $1 billion Star Wars-themed area that opens next year.

The following year, the city passed subsidies for luxury hotels, including the one planned by Disney.

Anaheim's outgoing Mayor Tom Tait, who regularly supported Disney in his long political career, voted against both measures. He said his views on subsidizing Disneyland changed because payments on $510 million of bonds the city issued under its 1996 agreement with Disney -- mainly for infrastructure to accommodate the Disneyland companion theme park, California Adventure -- were eating into its budget at a time of soaring pension liabilities.

Mr. Tait had also come to resent how the ticket-tax agreement could "tie the hands of generations of future voters."

Voter sentiment swung his way, ushering in the current anti-Disney city council majority in the 2016 election.

While the decision to cancel subsidies came with Disney's assent, some city council members feared the move could hamper growth. Mr. Tait had to plead for a "Kumbaya moment" amid fierce debate in city hall last month, before the council voted unanimously to dissolve the tax agreements. He declared it "a new chapter."

But many in Anaheim aren't ready to turn the page.

Council member Lucille Kring, who voted to cancel the agreements to avoid conflict with her colleagues, said she hopes incentives like the hotel subsidy will be restored under new leadership. "Even those who supported this are going to rue the day this happened in Anaheim," she said.

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Unions Focus Wage

Fight on Disney

Disney is at the center of a minimum wage ordinance on Anaheim's November ballot.

Labor unions representing Disneyland employees are campaigning in favor of a ballot measure facing voters that would require large hospitality businesses receiving tax rebates to raise their hourly minimum wage to $15 next year, with annual increases reaching $18 in 2022.

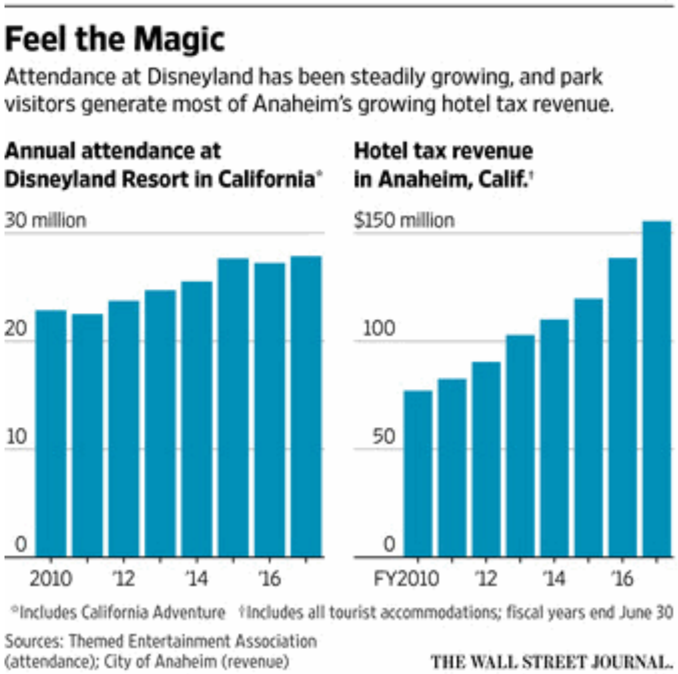
California's current minimum hourly wage of $11 is set to rise to $15 in 2022.

Because Anaheim recently agreed to cancel tax rebates that Disneyland previously enjoyed, city officials said they haven't yet studied whether Disney would qualify, given some remaining business agreements with the city.

That hasn't stopped unions from making Disney a centerpiece of their campaign promoting a mandatory wage increase.

Disneyland, which opposes the initiative, recently struck new agreements with unions under which it says about 80% of its 30,000 employees will be making at least $15 an hour by 2019.

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THE WALL STREET JOURNAL.
U.S. EDITION

**Business News: Investors Still Wary About Gold Miners**

By Paul Garvey
536 words
25 September 2018
The Wall Street Journal
J
B7
English


The mixed reaction to Monday's gold-mining megamerger underscores the challenges facing the North American gold sector, where shares have tumbled this year to discounts rarely seen outside significant market downturns.

Investors heartily applauded Barrick Gold Corp.'s agreement to buy Randgold Resources Ltd. for $6 billion in stock. Shares of Barrick gained 5.4% in New York and Randgold jumped 6% in London.

But most other gold-mining companies rose only modestly, highlighting the skepticism that Wall Street continues to hold for a sector hit hard in recent years by a flat gold price and concerns that some companies overextended themselves during the gold **bull market** that ended earlier this decade. Shares of AngloGold Ashanti Ltd. rose 0.6%, but Newmont Mining Corp. fell 1.5% in New York.

Shares of some of the biggest U.S.- and Canadian-listed gold-mining companies are trading at an average of around 0.75 times their net asset value, 28% below where they were a year ago, data from Macquarie tracking prices in the U.S. and Canada show.

Price to net asset value is a preferred measure for valuing mining companies because it takes into account variables such as the expected lifespan of mines and their output. The ratios are subjective and vary from analyst to analyst based on their assumptions.

A recent report by Bank of America showed that average price-to-NAV ratios were touching levels seen only fleetingly in 2013, when gold prices plunged, in the 2008 crisis, and around 2000 and 2001, when gold hit a low of $256 a troy ounce, compared with $1,199.30 Monday. Scotiabank estimates North American miners are trading at about half of the historical global average.

Bullion has fallen 12% since its 52-week high in January, but it isn't just gold prices that are weighing on the sector. North American mining companies' weak valuations reflect a continuing hangover from years of disastrous acquisitions and overleveraged balance sheets, as well as more recent blunders involving new mining projects.

While executives at Barrick Gold and Randgold Resources have focused on keeping costs in line and reining in debt, both are trading at steep discounts to net asset value following steady declines in their shares. Barrick's price-to-NAV has fallen to 0.8 times after its shares slumped 30% since the start of 2018 through Friday, while Randgold is trading at 0.6 times its NAV after its stock slid about 35% this year.

Joe Foster, portfolio manager of the $666 million Van Eck International Investors Gold Fund, said North American gold miners were still working to unwind reputational damage they inflicted on themselves during the mergers-and-acquisitions and development frenzy leading up to gold's peak at nearly $1,900 in 2011.

While some North American gold-mining companies have since improved their performance, by lowering operating costs, selling marginal assets and strengthening their balance sheets, they are unlikely to reclaim their traditional price premiums without some help from a gold price that is currently "stuck in the mud," Mr. Foster said.


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Document J000000020180925ee9p00012

THE WALL STREET JOURNAL.
U.S. EDITION

**Dozens of Stocks Feel Tariff Bite**

By Michael Wursthorn and Akane Otani
545 words
25 September 2018
The Wall Street Journal
J
B12
English


Dozens of stocks remain stuck in **bear-market** territory even as the U.S. **stock market** has charged to records, reflecting a disconnect that shows a robust economy hasn't offset trade jitters for many American conglomerates.

The trade fight has weighed particularly hard on shares of industrials and materials companies, which account for about one-fifth of the 80 stocks in the **S&P 500** that have tumbled at least 20% from their 52-week highs -- the common definition of a **bear market**.

Motorcycle manufacturer Harley-Davidson Inc., appliance maker Whirlpool Corp., tool company Stanley Black & Decker Inc. and machinery builder Caterpillar Inc. are among the biggest stocks that have slumped more than 20%, largely due to trade-related woes. Many companies that missed out on the broader rally have said trade tensions raised their costs, damped their profit outlooks or forced them to scrap projects.

Despite the stumbles, the market has recovered from the inflation- and trade-fueled **volatility** that put the nine-year rally on hold for most of 2018.

Investors have ranked a trade war as the top tail risk for four consecutive months, Bank of America Merrill Lynch said in its September survey of global fund managers. Fears that tighter trade policies could crimp growth also have hit fund managers' global outlooks, with 24% of investors expecting global growth to slow in the next year, up from 7% in August.

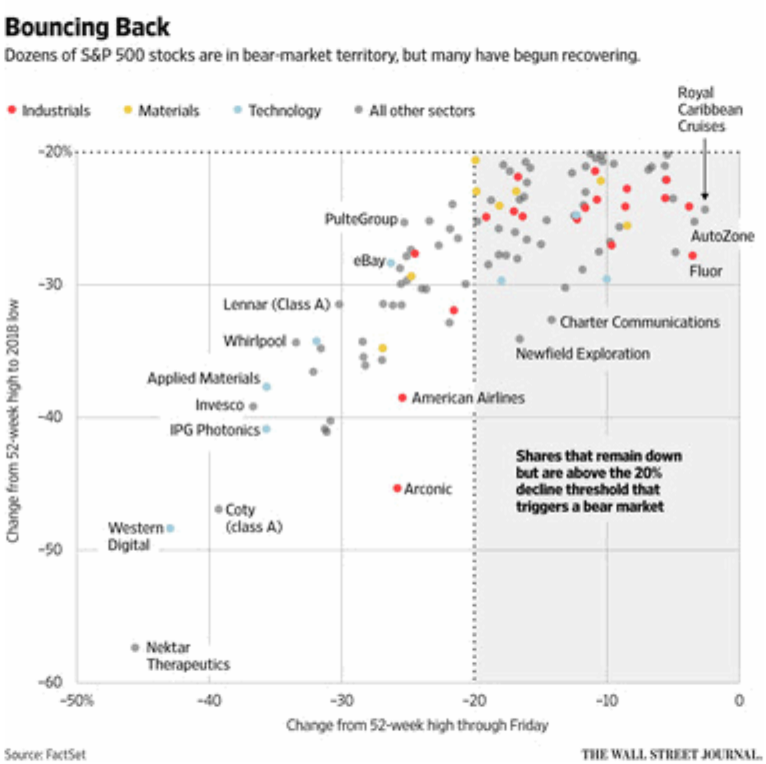
"There's a number of money managers who've been hesitant to be involved with the [companies] that are going to be potentially affected by the tariffs, whether they'll be able to export fewer goods or be buying less from China," said Mark Grant, managing director and chief global strategist at B. Riley FBR Inc.

Many of the firms that investors say have been most vulnerable to the trade rift fall in the industrial and materials sectors.

Among the hard-hit industrials stocks, engine maker Cummins Inc. is down 23% from its 52-week high after falling as much as 32%, hit by 25% tariffs on the small diesel engines and components it imports from its plants in China. Stanley Black & Decker, which has had to weigh replacing U.S. suppliers with foreign ones because of steel and aluminum tariffs, fell as low as 25% from its 52-week high and remains down 14%.

Auto makers and retailers that cater to drivers are another group of laggards. Ford Motor Co., down 28% from its 52-week high, earlier in the month scrapped plans to import its Focus vehicle to the U.S. from China. BorgWarner Inc. remains firmly stuck in **bear-market** territory and is down 13% so far this year. This month, the auto-parts supplier cut its earnings and sales outlooks for the year, citing weaker industry volumes in China, as well as "short-term issues" in Europe.

Shares of several tech manufacturers also have been crushed by tariffs on Chinese imports. Chip-equipment maker Applied Materials Inc. has seen its stock slide 37% from its March high. Lam Research Corp. and Western Digital Corp. shares have fallen more than 30% each from their trailing-year highs.

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THE WALL STREET JOURNAL.
U.S. EDITION

**Banking & Finance: Buoyant Markets Sting Bearish Hedge Funds**

By Laurence Fletcher
672 words
25 September 2018
The Wall Street Journal
J
B11
English


Nearly a decade into what feels like a never-ending **bull market**, it is getting awfully lonely for a group of maverick hedge funds betting on what they think will be a coming financial meltdown.

"If my analysis is right, we're past the point of no return," said Francesco Filia, founder of $500 million London-based Fasanara Capital, who has pivoted his $100 million macro fund to bet on a market crash. "Nothing else will do than having cash or shorts," he said.

So far, Mr. Filia's analysis has been painfully wrong. His fund has shrunk to around $100 million from around $160 million. Mr. Filia and his ilk believe a decade of central-bank bond buying, known as quantitative easing, has artificially inflated asset prices and created huge market distortions. Moves in the U.S. to raise interest rates and cut bondholdings and in the eurozone to stop QE could, they think, provide the catalyst for disaster.

It also has become an increasingly controversial trade as central banks have slowly tightened monetary policy without causing a crash.

Speculating against a widely held market consensus can mean a lonely -- and often painful -- road.

"Pretty much immediately when we went more **bearish** we started to see the funds going out," said Mr. Filia.

His bet lost money in some funds in 2016 and 2017 -- while the S&P has risen steadily. He blames a "sugar rush" as President Trump's tax cuts extended the **bull market**.

Crispin Odey, founding partner of Odey Asset Management, thinks the **bull market** is "old." He has been running an overall wager against stocks whereby his bets on falling prices -- including bets against Tesla and retail stocks -- have exceeded bets on rising prices by around 30%. That has contributed to three years of losses, including a loss of nearly 50% in 2016, although this year the fund is sharply up.

Clients have fled. His European fund, which was around 1.7 billion euros ($2 billion) four years ago, has shrunk to around 200 million euros.

Russell Clark, the main manager at London-based Horseman Capital, which runs more than $900 million, has been running a large position on falling U.S. stock prices including bets against technology and real-estate stocks. Quantitative easing is a "disastrous policy" because it can prove impossible to escape, he said.

Elliott Management Corp. told investors it was preparing for stocks and bonds to "take a notable dive."

But rather than talking about large outright negative bets, Elliott said it was preparing buy assets once they have fallen in price.

Mr. Filia became convinced around mid-2016 that risks in markets had grown. While the 2008 crash was centered around banks, risks today have moved to markets, Mr. Filia believes, which exist in a fragile state that is creeping closer to their breaking point. "Now we think the awakening from the QE sleep is going to be very violent."

His fund is positioned for a crash. One part bets on falls in stock and bond futures, while another two bet on stock and bond options. A fourth portion bets against exchange-traded funds, which he considers a key weak point in the financial system, when markets turn. A fifth part uses artificial intelligence to calculate when the market is likely to move sharply lower and then profit.

"I'm one of the few to be putting my money where my mouth is," he said.

Horseman's Mr. Clark thinks the U.S. corporate-bond market and **volatility**-selling markets are "unsustainable" and that investors' positioning in the face of slowing growth is "dangerous," according to letters to clients reviewed by The Wall Street Journal. He declined to comment.

Many investors have lost patience with performance. Mr. Clark was running $1.7 billion at the end of 2015. Redemptions have helped slash this to under $800 million.

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Rachael Levy contributed to this article.


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THE WALL STREET JOURNAL.
U.S. EDITION

Heard on the Street
**OPEC Lifts a Weight From Oil Prices**

By Spencer Jakab
437 words
25 September 2018
The Wall Street Journal
J
B13
English


[Financial Analysis and Commentary]

Sunday's long-winded press release from the meeting of 20 oil exporters in Algiers would have taken 10 tweets to bang out. While it was considerably less punchy than President Trump's 219-character missive on Thursday to OPEC, the announcement had a lot more impact: International **oil prices** rose to their highest level in nearly four years.

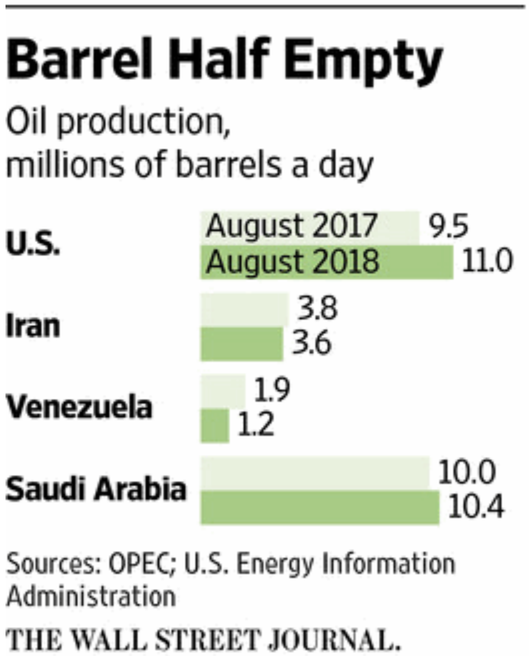
The decision to essentially wait and see on raising output more quickly isn't so much a rebuke to the White House as further evidence that the petroleum market is complicated. It is even more complicated than usual at the moment. The movers and shakers in the joint committee guiding production are focused on issues other than the optics of rising American pump prices before midterm elections.

Demand for oil remains robust, supported by a humming global economy, but in the past few months three constraints involving supply have all gotten a bit worse. One is that Venezuela's social collapse continues unabated. Oil output is at multidecade lows, currently at just 1.24 million barrels a day.

Total U.S. crude output surged by a staggering one million barrels a day between June 2017 and June 2018. Since then, though, it has barely budged despite improving cash flows. Whatever price incentives exist, pipeline constraints and other logistical challenges will slow gains until mid or late 2019.

Finally, there is Iran. The last time sanctions were imposed, exports fell sharply but there were still buyers for Iranian crude in Asia. Total production averaged just under 2.8 million barrels a day in 2014, compared with 3.8 million in the second quarter of this year. Production fell by nearly 300,000 barrels a day as of August, which was surprising because expectations when sanctions were imposed was that production would fall just 500,000 a day. That estimate now may be too low as more-aggressive sanctions begin in November. A bigger decline could put a serious squeeze on global supply.

Saudi Arabia and Russia can fill some of the emerging gap, but there are political reasons for them to allow prices to stay high. Even with Brent now about $80 a barrel, many smaller OPEC producers are hurting economically and need to replenish their coffers. The fact that the producers' communique sees "an overall healthy balance between supply and demand" signals that output will ramp up slowly, setting the market up for at least a temporary period of high prices and presidential ire.



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Document J000000020180925ee9p00019

The New York Times

Business/Financial Desk; SECTB
**Faltering Trade Talks Send Shares Slightly Lower**

By THE ASSOCIATED PRESS
646 words
25 September 2018
The New York Times
NYTF
Late Edition - Final
6
English


Global stocks took small losses on Monday after China reportedly pulled out of trade talks with the United States. Industrial companies and banks suffered some of the worst declines among American stocks.

The United States and China officially began taxing larger amounts of each other's goods on Monday, and The Wall Street Journal reported that China had pulled out of talks that could have led to a new round of negotiations to end the trade war.

The United States is now taxing another $200 billion in Chinese imports at a rate of 10 percent, and China added taxes of 5 to 10 percent on $60 billion in American products. **Oil prices** jumped after OPEC decided not to produce more oil.

Technology and health care companies rose, leaving United States indexes only slightly lower.

''The market's been remarkably resilient over the last couple of months while trade tensions were heating up,'' said Terry Sandven, chief equity strategist at U.S. Bank Wealth Management.

Sandven said that the trade spat would endure past the midterm elections in November but that stocks were likely to keep rising because of strong earnings growth for American companies, combined with low inflation and low interest rates.

The **Standard & Poor**'**s 500**-**stockindex** fell 10.30 points, or 0.4 percent, to 2,919.37. The **Dow Jonesindustrial average** lost 181.45 points, or 0.7 percent, to 26,562.05. Both the **S**.**&P**. **500** and the Dow set record highs last week.

The Russell 2000 index of smaller-company stocks dropped seven points, or 0.4 percent, to 1,705.32. The **Nasdaq composite** rose 6.29 points, or 0.1 percent, to 7,993.25.

After a **volatile** stretch early this year, the S.&P. hasn't risen or fallen 1 percent in a day since late June.

Sandven noted that this year's gains have been concentrated in technology, retail and health care companies. That was the case Monday, as Apple gained 1.4 percent to $220.79 and Abbott Laboratories, which makes drugs and infant formula, advanced 3.5 percent to $71.44. Sandven said it would be an encouraging sign for the market if other sectors did better.

Investors in the United States were occupied with other news. OPEC and its key allies, like Russia, decided not to increase their oil output further. Production is falling in some OPEC nations, including Iran, which faces new sanctions from the United States.

Benchmark United States crude gained 1.8 percent to $72.08 a barrel in New York, while Brent crude, the international standard for **oil prices**, rose 3 percent to $81.20 a barrel in London, its highest price in more than three years.

Airlines and other transportation companies fell as investors anticipated that they would have to pay higher prices for fuel.

Late Friday, Comcast won an auction for majority control of Sky, the British satellite TV giant. Its final offer was worth about $39 billion and topped an offer from 21st Century Fox, which was already a major Sky shareholder.

In London, Sky shares jumped 8.6 percent. Comcast sank 6 percent to $35.63, while Fox rose 1.5 percent to $45.01. Disney, which is buying Fox, climbed 2.1 percent to $112.77.

**Bond prices** fell. The yield on the **10**-**year Treasury** note rose to 3.09 percent from 3.07 percent.

Gold rose to $1,199.30 an ounce. The dollar rose to 112.78 yen. The euro fell to $1.1744 from $1.1747.

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

CHART: The **S**. **& P**. **500 Index**: Position of the **S**. **& P**. **500 index** at 1-minute intervals on Monday. (Source: Reuters)

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THE WALL STREET JOURNAL.
U.S. EDITION

**Resurgent Russia Takes Lead in Wheat --- Exports are soaring as nation's farms emerge from decades of neglect**

By James Marson
1,935 words
24 September 2018
The Wall Street Journal
J
A1
English


Corrections & Amplifications

In September, **oil prices** were down about 30% from their high in 2014, after recovering from a swoon of about 77%. A Page One article on Sept. 24 about Russia's dependence on wheat exports incorrectly said that **oil prices** at the time were down 25% from their high in 2014, after recovering from a swoon of more than 60%.

(WSJ November 21, 2018)

(END)

OTRADNAYA, Russia -- Vladimir Mishurov transformed the remnants of the "Lenin's Path" collective farm in this village into a profitable business. He also helped make Russia the world's largest wheat exporter for the first time since the last years of the czars.

Over the past decade or so, Mr. Mishurov replaced his aging Russian equipment with a dozen high-tech machines from John Deere and other makers, and started using powerful new fertilizers and seeds. He bought and rented more acres from neighbors and family, eventually reaching about 3,600, taking advantage of Russia's overall low prices for land.

And as many farmers do in the U.S., he often worked days on end with little sleep, especially during the harvest.

The major difference between Mr. Mishurov and a farmer on America's Great Plains: The Russian's costs are lower, and mostly in rubles, making his overseas sales -- priced in dollars -- immensely more valuable.

Amid a multiyear, brutal slump in grain prices, Russian agriculture is thriving. The country exported more than 40 million tons of wheat in the year ending June, around 50% more than the previous year, and the highest level for any country in the past quarter-century. Russia overtook the U.S. as the world's biggest exporter of wheat in 2016, and again beat the U.S. in 2018.

The growing Russian competition is one more pressure point threatening American farming, which is facing the biggest wave of farm closures in the U.S. since the 1980s. A global oversupply of grain has pushed prices down to around half the level in 2012, when prices peaked, making it difficult to turn a profit in dollars.

U.S. trade disputes with China and other countries could make Russian wheat even more attractive, if big buyers apply retaliatory tariffs to U.S. grains. China has added a 25% tariff on U.S. wheat, but Chinese restrictions on imports from Russia have prevented Moscow from taking advantage yet, according to Swithun Still, director at Switzerland-based Solaris Commodities SA, which trades Russian grain.

For now, "it's not the trade war, it's economics" that is helping Russian wheat compete, even in places close to the U.S. such as Mexico, Mr. Still said. Russian "quality got better, and it's cheaper."

Russian farmers come out ahead when export earnings are converted into rubles. Since the Russian currency has depreciated, a dollar now converts to twice as many rubles as it did in 2014. Russia has a similar advantage against the euro and other currencies. Russian farmers can cover their costs at home to keep planting, and also undercut Western competitors on price.

Russia's surge of agriculture exports, including grains, fish and meat, is part of an effort to diversify the economy away from crude oil. Oil and natural gas were once the source of half of federal budget revenues. With **oil prices** still down 25% from their high in 2014 -- recovering from a swoon of more than 60% -- exports now account for around 40% of budget revenues.

"Given the fall in prices for oil, grain has come to the fore. Grain is our oil," then-Agriculture Minister Aleksandr Tkachev said in 2016.

Less-expensive Russian wheat is pushing U.S. and European grain out of import-dependent countries in the Mideast and North Africa, where the Kremlin has made a military and diplomatic push for influence in recent years.

Agriculture exports, at $20.7 billion in 2017, have overtaken the arms industry as Russia's No. 2 earner. Wheat makes up about a quarter of the total.

Russia harvested an area of wheat almost twice as large as the U.S. in the year ended in June, according to the U.S. Department of Agriculture. American farmers, seeing little opportunity to profit, planted the smallest area of wheat since records began a century ago. U.S. wheat production shrank 25% in the year.

Mr. Mishurov's farm is on the fertile steppe of southern Russia. The area is the country's biggest grain producer -- a bread basket known for its mineral-rich black earth and mild climate.

Now 46 years old, he spent his late teens and early 20s driving a bone-rattling tractor that needed its motor refurbished every year and left his hands callused. A lack of cash meant workers were paid in sacks of flour, wheat or sugar, and drunkenness was pervasive.

At the start of the 20th century, Russia had been the world's largest exporter of wheat. The Soviets killed and imprisoned millions, including many of the most-successful farmers, as part of an effort to install a system of collective farming that proved inefficient. By the 1970s, the Soviet Union had to import grain.

Collective farms stumbled on after the Soviet Union collapsed in 1991, often still managed by the same bosses without business smarts or cash to invest.

"No one was in charge," said Mr. Mishurov. "They couldn't adapt to the market economy. They were accustomed to unthinkingly following instructions."

Farmhands worked "to pass the time of day until they could go home," said Andrei Burdin, a farmer from a nearby village who works land that was once part of the "Dawn of Communism" collective farm. "Farming was at a dead end."

Russia opened the land market at the end of the 1990s, but new investors and their managers tended to be far from the land and averse to risks, farmers said.

Mr. Mishurov, who worked as chief agronomist at a large farming conglomerate, recalled telling an executive in the early 2000s that using pesticide could increase the barley crop by around a quarter.

" 'No, Vova, it's enough already,' " he said the executive replied, using a nickname. "Why should I persuade someone to earn more money?" Mr. Mishurov said.

He struck out on his own in the mid-2000s. At first, he pooled land with relatives and used whatever equipment he could lay his hands on. Today, he grows wheat, barley, beets, corn, sunflowers, peas and other crops.

Mr. Burdin, 43, started farming around 250 acres in 2005 with a dilapidated tractor and planter. He invested early profits into more-efficient vehicles and better fertilizer, and expanded territory by renting from neighbors.

"When we made the first money, I didn't buy a Mercedes or an apartment," he said. "I put it into the next season."

At first, he bought Russian equipment, but later upgraded to John Deere tractors and combines, which the Russians call zelyonaya tekhnika, or "green machines." Mr. Burdin said he tested a John Deere combine against a Russian one and found it produced about one-third more grain from the same area.

He also added a planter from Sweden's Vaderstad AB that shoots seeds into the ground at the optimal depth and intervals, improving yields. He now farms about 3,700 acres.

 

In April, while loading the planter with seed, Mr. Burdin joked with farmhands about equipment in the old days. He recalled working with a pesticide sprayer that would soak him with chemicals. He said he could only work for about four hours at a time before giving up, out of fear for his health. Now, his sprayer can measure how much pesticide to spray and where, keeping costs down.

The price of land in the region where Messrs. Mishurov and Burdin live is significantly lower than for many foreign rivals. On average, farmland in Romania, a European Union member on the Black Sea, is nearly three times the price, while farmland in Iowa and Kansas is more than five times the price, according to a 2017 survey by Moscow-based SovEcon, which provides consulting services, analysis and forecasts on Russian agriculture.

Mr. Burdin said Russian seeds and fertilizers still cost less than Western brands, even though they have improved significantly in recent years. He buys wheat seeds from a state-run agricultural institute, and can plant the seeds produced from those plants the next season. Many American farmers use expensive, high-yield, patented seeds from companies such as Bayer AG or DowDuPont Inc., which don't allow the produced seeds to be planted, requiring farmers to buy fresh seeds annually.

Transport costs are also low for the region. It is close to Black Sea ports, and gasoline costs are much lower than in Western Europe. Mr. Burdin and Mr. Mishurov run their own fleets of trucks that move grain to the Novorossiysk port some 200 miles away by road.

Private and state-owned companies have modernized grain terminals in recent years and increased their capacities. Farmers can use an app on a smartphone to book a slot for their trucks to deliver grain, rather than the old system of having trucks wait in line for days.

Bumper harvests are stretching infrastructure. Windows for unloading grain are snapped up quickly, and farmers are often assigned slots several days after a requested time, Mr. Burdin said.

Exports "could be even higher if they could figure out how to load more," he said.

Russia has made it a priority. President Vladimir Putin ordered officials to tackle infrastructure bottlenecks that are holding back exports. In inland areas, large distances and a lack of train cars and storage silos hamper grain from reaching external markets.

One of Russia's largest terminals in Novorossiysk is completing a three-year modernization this year that will nearly double its capacity. Other companies have announced plans to build or expand terminals on the Black Sea, the Baltic Sea in the north and in the Far East. Officials said expansions at ports could increase export capacity of grains by 50% to 7.5 million tons a month by 2020.

Government officials tout the importance of state subsidies, including inexpensive loans to help farmers replace old equipment. Analysts and farmers say the state's efforts to support agriculture have been hit and miss. Subsidies often make their way to well-connected companies, investment in infrastructure has been slow and bureaucrats and other officials often expect bribes.

"Farmers received the freedom to do business in the way they thought most efficient," said Andrei Sizov Jr., managing director of SovEcon. "The role of the state was quite muted in the last 10 years, and that was good for the industry."

Giant agroholdings, conglomerates often created by wealthy tycoons or people close to top federal and regional government officials, have built up spreads that dwarf Western farms. Individual farms larger than 250,000 acres, or nearly 400 square miles, account for around 13% of all land farmed in Russia, according to Mr. Sizov.

Mr. Mishurov can now afford to collect and restore a half-dozen vintage Soviet cars and vacation in the Maldives and Thailand, although he said he prefers staying home.

The poor villages here depend on the generosity of wealthier farmers. Mr. Mishurov funded renovations to his village's statue of Lenin and a monument to locals who died in World War II, while Mr. Burdin paid to fix up his village's kindergarten.

Mr. Mishurov employs 10 farmhands, three guards and a cook who prepares meals for the workers. "It's a lot for our acreage, but we try to preserve jobs in the village," he said. One recent morning, a man dropped by Mr. Mishurov's farmyard office to cadge a bucket of corn for his hens. It was a former collective farm boss.

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WSJ PRO CENTRAL BANKING

Markets

**Policy Makers Rethink a 2% Inflation Target; Big debate now for central bankers is what would be a better target**

By Tom Fairless
1,125 words
23 September 2018
10:04 PM
WSJ Pro Central Banking
RSTPROCB
English


What's so special about 2% inflation?

From Ottawa to Oslo, policy makers have been considering whether that level of consumer-price growth, a Holy Grail for the world's major central banks over the past quarter-century, is still relevant.

The 2% target was always an arbitrary figure, some economists argue, and even if it was optimal two decades ago, that is no longer the case given deep changes that have since reshaped the global economy.

Trouble is, it isn't clear what inflation rate would be better. Dozens of academic studies that considered that question have produced answers ranging from 6% to less than zero, according to a survey published last year by Federal Reserve economist Anthony M. Diercks. While deflation, or steadily falling prices, are generally considered to weigh on economic growth, a mildly negative inflation rate would also have benefits, such as eliminating the cost of holding cash.

The debate has gained traction since former Federal Reserve Chairwoman Janet Yellen suggested last year that the U.S. central bank might revisit its 2% inflation target. Canadian officials have also suggested they might be open to changing the Bank of Canada's 2% target when its mandate comes up for review in 2021.

Recently, economists have tended to call for a higher target. The main argument: That would give central banks more room to fight economic downturns because higher inflation implies higher interest rates, thus giving the Fed more room to cut.

"Whatever [inflation] rate was thought to be optimal in 2006 or before is now too low," says Olivier Blanchard, a senior fellow at the Peterson Institute for International Economics in Washington, D.C., who has called for a 4% target.

Factors such as aging populations, low economic growth and higher savings rates are working to push down the neutral interest rate, at which the economy is growing at a sustainable rate for the long run and inflation is stable. As a result, central banks run a greater risk of taking benchmark interest rates to zero or below when seeking to support growth.

And yet, Norway's government said recently it would reduce its central bank's inflation target, to 2% from 2.5%, arguing there was no longer any reason to diverge from international norms. With inflation near target, the central bank raised interest rates to 0.75% on Sept. 20.

The case for a higher target runs like this: Policy makers find it difficult to cut benchmark interest rates much below zero. If inflation is 2%, that means central banks can reduce the real interest rate—the benchmark rate minus inflation—to minus 2% by cutting the benchmark rate to zero. If inflation were higher, say 4%, cutting the benchmark rate to zero would push the inflation-adjusted rate to minus 4%, providing an extra kick for the economy.

Higher inflation could have other benefits. It could help economies adjust after a downturn by lessening the need for outright wage cuts, because rising prices will erode wages anyway. It could also make it easier for borrowers to pay down debt, though that is something that lenders historically have always resisted. A 2009 study estimated that U.S. inflation of 6% for four years could reduce the nation's debt-to-GDP ratio by around 20 percentage points, similar to what happened after World War II.

Other economists have cast doubt on whether that level of inflation would reduce the debt ratio by so much. And many worry that central banks would struggle to push inflation to 6% anytime soon, given how hard it was to hit 2%.

Vítor Constâncio, the European Central Bank's vice president back in May, said at the time that while he had "no theoretical objections" to a "mild" upward revision of the inflation target, moving to a new target could undermine central banks' hard-won credibility.

The ECB is among a group of central banks that have reduced benchmark interest rates below zero, a novel move aimed at providing extra stimulus to their economies. Former Fed Chair Ben Bernanke has suggested that negative rates might be a better alternative to higher inflation targets.

"Yes, negative interest rates raise a variety of practical problems, as well as political and communications issues, but so does a higher inflation target," Mr. Bernanke wrote in a 2016 blog post. "In the political sphere, the fact that negative rates would be temporary and deployed only during severely adverse economic conditions would be an advantage."

Higher inflation can have drawbacks, as many economies have learned through painful experience. It could distort the tax system and mask economic signals, such as whether goods are rising in price because they are scarce. Banks might demand an inflation-risk premium when granting long-term loans, because high inflation can lead to more **volatile** price movements, says Michael Schubert, an economist with Commerzbank in Frankfurt. Thus, financing would become more expensive, causing companies to invest less.

Crucially, an inflation rate of 2% allows households and businesses to largely disregard price increases. That effect might be lost if inflation is allowed to rise much higher.

"We know that some number higher than a 2% to 3% rate of inflation will materially enter decision-making, because we have had plenty of experience of higher rates of inflation that demonstrates that," says Guy Debelle, deputy governor of Australia's central bank. "How much higher though, we don't really exactly know."

One possible solution: Central banks could allow inflation to rise a bit above 2% without aggressively trying to bring it down. That could give them more room for maneuver, and gradually inflate away some of the world's enormous debt load.

It seems to already be happening in the U.S., where inflation in August was 2.7%. The Fed has been raising rates, but only gradually, and doesn't seem likely to step up its pace.

Although eurozone inflation has accelerated in recent months and is now 2%, the ECB has signaled that it won't raise rates for about a year.

Joseph Gagnon, a fellow at the Peterson Institute, says the Fed "ought to tilt policy toward overshooting, not for its own sake, but to avoid" undershooting its target again in future.

Mr. Fairless is a Wall Street Journal reporter in Frankfurt. Email: tom.fairless@wsj.com.

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THE WALL STREET JOURNAL.

Markets

**Meet the Bear-Market Stocks Hiding in S&P 500's Record Run; The shares reflect a disconnect that shows a robust economy hasn't offset trade jitters for many American conglomerates**

By Michael Wursthorn and Akane Otani
1,137 words
24 September 2018
06:02 PM
The Wall Street Journal Online
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English


Corrections & Amplifications

Applied Materials is a chip-equipment maker. An earlier version of this article incorrectly described the company as a chip maker. (Sept. 26, 2018)

Dozens of stocks remain stuck in **bear-market** territory even as the U.S. **stock market** has charged to records, reflecting a disconnect that shows a robust economy hasn't offset trade jitters for many American conglomerates.

The trade fight has weighed particularly hard on shares of industrials and materials companies, which account for about one-fifth of the 80 stocks in the **S&P 500** that have tumbled at least 20% from their 52-week highs—the common definition of a **bear market**.

Motorcycle manufacturer Harley-Davidson Inc., appliance maker Whirlpool Corp., tool company Stanley Black & Decker Inc. and machinery builder Caterpillar Inc. are among the biggest stocks that have slumped more than 20%, largely due to trade-related woes. Many of the companies that missed out on the broader rally have said trade tensions have raised their costs, damped their profit outlooks or forced them to scrap projects.

Despite the stumbles, the broader market has recovered from the inflation- and trade-fueled **volatility** that put the nine-year rally on hold for most of 2018. The **S&P 500** closed Friday a whisker short of Thursday's record, while the **Dow Jones Industrial Average** ended at an all-time high, finishing its best week since mid-July.

Investors have ranked a trade war as the top tail risk to the markets for four consecutive months, Bank of America Merrill Lynch said in its September survey of global fund managers. Fears that tighter trade policies could crimp growth also have hit fund managers' global outlooks, with 24% of investors expecting global growth to slow in the next year, up from 7% in August.

"There's a number of money managers who've been hesitant to be involved with the [companies] that are going to be potentially affected by the tariffs, whether they'll be able to export fewer goods or be buying less from China," said Mark Grant, managing director and chief global strategist at B. Riley FBR Inc.

Many of the firms that investors say have been most vulnerable to the trade rift fall in the industrial and materials sectors.

Among some of the hard-hit industrials stocks, engine maker Cummins Inc. is currently down 23% from its 52-week high after falling as much as 32%, hit by 25% tariffs on the small diesel engines and components it imports from its plants in China. Stanley Black & Decker, which has had to weigh replacing U.S. suppliers with foreign ones because of steel and aluminum tariffs, fell as low as 25% from its 52-week high and remains down 14%.

Materials companies, meanwhile, have suffered as the cloudy outlook for global growth has sent copper prices lower. Newmont Mining Corp. has fallen 26% from its high, while Freeport-McMoRan Inc. has lost 29%.

Auto makers and retailers that cater to drivers are another group of laggards. Ford Motor Co., down 28% from its 52-week high, earlier in the month scrapped plans to import its Focus vehicle to the U.S. from China. BorgWarner Inc. remains firmly stuck in **bear-market** territory and is down 13% so far this year. This month, the auto-parts supplier cut its earnings and sales outlooks for the year, citing weaker industry volumes in China, as well as "short-term issues" in Europe.

Shares of several tech manufacturers also have been crushed by tariffs on Chinese imports. Chip-equipment maker Applied Materials Inc.—which said the Trump administration's tariffs will result in "unnecessary costs" that cause "economic harm" at a congressional hearing in July—has seen its stock slide 37% from its March high. Lam Research Corp. and Western Digital Corp. shares have fallen more than 30% each from their trailing-year highs.

To be sure, some of the stocks that have fallen into **bear-market** territory, like bricks-and-mortar retailers, have struggled because of industrywide pressures—things that have had little to do with trade. General Mills Inc., down 27% from its trailing year high, has struggled to reverse stagnating sales as consumers have abandoned its snacks and yogurt offerings for brands offering healthier alternatives. J.M. Smucker Co. has faced similar pressures; its shares fell as low as 23% from their 52-week highs and remain down 17%.

Still, even with dozens of stocks struggling to break out of **bear-market** territory, the U.S. **stock market** remains well above its peers.

Hong Kong's Hang Seng Index fell into **bear-market** territory earlier this month and remains down 8.1% for the year, with trade concerns and a stronger U.S. dollar hurting the index and other developing economies. China's benchmark Shanghai Composite and MSCI's flagship emerging-markets index both have suffered drawdowns of more than 20% from recent highs.

One reason why the U.S. **stock market** has been able to keep driving higher is that investors have bet on a handful of dominant technology companies weathering the fallout from tighter trade policies.

Shares of Apple Inc. and Amazon.com Inc. are responsible for nearly 30% of the **S&P 500**'s 9.2% gain so far this year, according to S&P Dow Jones Indices.

However, analysts caution that while investors have been pricing the risk of a trade war into shares of manufacturers, mining firms, home builders and others, they mostly have ignored the glaring risks associated with major tech companies, such as potential punitive measures that could affect Apple's manufacturing in China or cost increases that could hurt Amazon's e-commerce sales. That puts the **S&P 500**'s narrow leadership at risk of a sharp pullback if trade tensions reach a boiling point, similar to the swift correction that stocks suffered in February on worries about a potential pickup in inflation.

Those companies have already showed some signs of stress in recent sessions due to concerns of new government regulation and the potential impact protectionist policies could have on tech manufacturers. Tech stocks in the **S&P 500** are down 0.9% in September, on pace for their biggest monthly loss since March.

Apple is "the No. 1 company exposed to trade," said Michael O'Rourke, chief market strategist for JonesTrading LLC. "Until people see the definite negative out there, people will ride this market out as long as they can. That's representative of a very large problem."

Write to Michael Wursthorn at Michael.Wursthorn@wsj.com and Akane Otani at akane.otani@wsj.com

More

* Stocks Drop as Hopes for a Trade Truce Fade

* U.S. Stocks Close at Records (Sept. 20)

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THE WALL STREET JOURNAL.

Markets

**Despite Big Merger, Investors Still Cautious on Gold Mining Companies; Merger of Barrick Gold and Randgold draws muted reaction, highlighting the skepticism that Wall Street still holds for the North American gold sector**

By Paul Garvey
870 words
24 September 2018
11:39 AM
The Wall Street Journal Online
WSJO
English


The mixed reaction to Monday's gold-mining megamerger underscores the challenges facing the North American gold sector, where shares have tumbled this year to discounts rarely seen outside significant market downturns.

Investors heartily applauded Barrick Gold Corp.'s agreement to buy Randgold Resources Ltd. for $6 billion in stock. Shares of Barrick rose 6% and Randgold climbed 7%.

But other gold-mining companies rose only modestly, highlighting the skepticism that Wall Street continues to hold for a sector hit hard in recent years by a flat gold price and concerns that some companies overextended themselves during the gold **bull market** that ended earlier this decade. Shares of AngloGold Ashanti Ltd rose 1.4% and Newmont Mining Corp. was flat.

Shares of some of the biggest U.S.- and Canadian-listed gold-mining companies are trading at an average of around 0.75 times their net asset value, 28% below where they were a year ago, data from Macquarie tracking prices in the U.S. and Canada show.

Price to asset value is a preferred measure for valuing mining companies because it takes into account variables such as the expected lifespan of mines and their output. The ratios are subjective and vary from analyst to analyst based on their assumptions.

A recent report by Bank of America showed that average price-to-NAV ratios were touching levels seen only fleetingly in 2013, when gold prices plunged, in the 2008 crisis, and around 2000 and 2001, when gold hit a low of $256 a troy ounce, compared with $1,207 Monday. Scotiabank estimates North American miners are trading at about half of the historical global average.

Bullion has fallen 12% since its 52-week high in January, but it isn't just gold prices that are weighing on the sector. North American mining companies' weak valuations reflect a continuing hangover from years of disastrous acquisitions and overleveraged balance sheets, as well as more recent blunders involving new mining projects.

Among the gold-mining companies with the weakest valuations, Centerra Gold Inc. is trading at roughly 0.5 times its NAV, according to the Macquarie data, after its shares fell 21% this year. Detour Gold Corp.'s price-to-NAV is at about 0.6, the data show, with the stock down 28% this year.

Barrick Gold and Randgold Resources have been hit as well. While executives at the two companies have focused on keeping costs in line and reining in debt, both are trading at steep discounts to asset value following steady declines in their shares. Barrick's price-to-NAV has fallen to 0.8 times after its shares slumped 30% since the start of 2018, while Randgold is trading at 0.6 times its NAV after its stock tumbled about 35% this year.

Joe Foster, portfolio manager of the $666 million Van Eck International Investors Gold Fund, said North American gold stocks were still working to unwind reputational damage they inflicted on themselves during the mergers-and-acquisitions and development frenzy leading up to gold's peak at nearly $1,900 in 2011.

"All these companies during the boom years, they were building projects that didn't generate good returns and blowing out their balance sheets and taking on too much debt," said Mr. Foster. "The companies were very poorly managed, and they really fell out of favor."

While some North American gold-mining companies have since improved their performance, by lowering operating costs, selling marginal assets and strengthening their balance sheets, they are unlikely to reclaim their traditional price premiums without some help from a gold price that is currently "stuck in the mud," according to Mr. Foster.

He said Barrick, along with Newmont Mining, Agnico Eagle Mines Ltd. and B2Gold Corp., had "cleaned up their balance sheets" and are "building projects with good returns."

Part of the problem is that dividends tend to be almost an "afterthought" among North America's gold stocks, according to Shree Kargutkar, a portfolio manager at Sprott Asset Management.

In contrast, the dividends that have become a regular feature of the Australian gold companies show not only the health of their mines but a determination by management to remain disciplined and reward shareholders along the way.

Australia's gold miners have also been insulated from the full impact of the falling gold price due to the simultaneous fall in the nation's currency, which has protected them from much of the tumult affecting overseas rivals. Australia is the world's second-biggest gold producer after China, where few gold-mining companies are publicly listed.

Producers from Australia are trading at more than one times their NAV. Mr. Foster said North American gold companies had historically traded at a premium to their Australian rivals.

"Those valuations have flipped, and we've never seen that before," he said.

Write to Paul Garvey at paul.garvey@wsj.com

More

* Gold Giant Barrick Agrees to Buy Randgold for $6 Billion

* Analysis: Barrick Gold May Need to Polish Up Its Offer

Document WSJO000020180924ee9o004h5

 

THE WALL STREET JOURNAL.

World

**Europe Hopes Oil Demand From China, India and Turkey Will Keep Iran in Nuclear Deal; With U.S. sanctions forcing European companies to abandon the Islamic republic, Iran's continuance may depend on non-European purchases**

By Ian Talley in Washington and Laurence Norman in Brussels
1,402 words
24 September 2018
11:47 AM
The Wall Street Journal Online
WSJO
English


Corrections & Amplifications

Foundation for the Defense of Democracies is a Washington-based think tank. An earlier version of this article incorrectly spelled the think tank's name. (Sept. 24, 2018)

With European companies abandoning Iran in the face of growing U.S. pressure, European politicians backing Iran are counting on oil demand from China, India and Turkey to keep the 2015 nuclear deal alive.

Since the U.S. withdrawal from the nuclear deal in May, Iran has threatened to resume its nuclear program if it loses economic benefits from the deal, which saw most international sanctions lifted. Iranian officials say they could start enriching uranium at banned levels within days.

European officials continue studying ways to counter renewed U.S. sanctions and shield their companies from U.S. penalties. They hope to keep cash and trade flowing to Iran so it would remain in a deal meant to forestall its development of nuclear weapons.

But Western officials say that the impact of any European measures is likely to be modest and that Tehran's decision to stay in the pact after U.S. sanctions fully kick in on Nov. 5, may hang on the willingness of the oil exporter's biggest non-European clients to keep buying crude.

If Tehran can foresee weathering U.S. pressure until 2020, European thinking goes, American voters might elect a new president who could reverse course.

For most European companies, keeping a hand in Iran's $400 billion economy at the risk of losing access to the $20 trillion U.S. economy and being cut off from the Western financial system doesn't make business sense.

"It's in their economic self-interest to comply," said Brian Hook, the State Department's special representative for Iran. "We didn't really need to do much coaxing for these companies and banks."

In the first four months of the administration's two-phase sanctions rollout, nearly half of the 67 Fortune Global-500 companies invested in Iran before May pulled out or signaled imminent exit. Many of the largest are European.

Germany's insurance giant Allianz SE and industrial conglomerate Siemens AG are closing operations. France's oil major Total SA and car-maker Peugeot said they are exiting, as did Denmark's shipping titan A.P. Moeller-Maersk A/S. Austria's Oberbank AG, which signed a $1.2 billion financing deal with 14 Iranian banks last year, is cutting ties.

Others that have said they plan to defy U.S. sanctions may reverse course ahead of the November deadline, when the most punishing prohibitions kick in.

Exports to Europe of Iran's most critical revenue source—crude oil—dropped by more than one-third between May and August, before the ban on oil trade even starts. Analysts and officials predict buying will continue dwindling.

European officials, led by France, Britain and Germany, have sought to stem the reduction in economic ties. Among the ideas still being worked on is creating a new sovereign financial channel with no links to the U.S. financial system to allow payments to and from European companies in Iran. There have also been discussions on allowing Iranian banks to open or reactivate accounts in European central banks.

However, officials admit that U.S. sanctions could target officials involved in the schemes. Banks receiving money from the financial channel could also be hit by U.S. authorities for helping evade U.S. sanctions.

Iran's foreign minister, Javad Zarif, was set to press the issue Monday in a meeting with counterparts from the five remaining parties to the 2015 pact: Russia, China, France, Britain and Germany. On Wednesday, President Trump will chair a session at the United Nations General Assembly that he wants to focus on what U.S. officials call Iran's malign activities.

A senior European diplomat said that while the economic impact of European measures to maintain commerce may prove "marginal," the political signal is important. "We are buying time" the diplomat said, "We just hope it will convince the Iranians not to make a stupid decision."

European officials believe many Iranian policy makers see little advantage in abandoning the deal. It would escalate tensions with the U.S. and force Europe and others to reimpose their own sanctions.

But Iran's oil export numbers after November may change Tehran's calculus, they say, particularly in the current **volatile** atmosphere. Tensions between the U.S. and Iran are flaring over Syria, Yemen and Iraq. In recent days, Iran has blamed the U.S. and its allies for a terrorist attack that left 25 people dead.

President Hassan Rouhani's government is under mounting political strain, fueled by a shaky economy that has seen Iran's currency repeatedly plumb new depths.

More than one in 10 Iranian workers is unemployed. Prices are spiraling out of control, surging 20% between June and July.

The Trump White House is seeking to replicate the sanctions campaign the Obama administration orchestrated against Iran from 2011 as Tehran expanded its nuclear program. With European help, Iran's oil exports fell 60% by 2014—more than 1.5 million barrels a day—and Iran's economy tanked.

Eyeing that breaking point, the Trump administration's plan was more ambitious, giving countries a six-month window to slash purchases at a steeper rate. Adding to the pressure on Iran, **oil prices** are lower than during the Obama era.

The plan is hurting Iran. Cuts from Iran's major clients, including China, India and Japan, are in line to hit 900,000 to 1.2 million barrels a day by November from the May start, according to some analysts.

"We are working with all countries, including China, to get them to zero," Manisha Singh, the U.S. assistant secretary of state overseeing sanctions policy, told lawmakers last week. "We are prepared to take the strongest actions possible on people who will not assist us."

The Trump administration aims to force Iran to negotiate a more wide-ranging deal that includes restraints on its regional interference and ballistic-missiles program. For now, Iran says it is not interested.

Even if talks prove elusive, the U.S. hopes that choking Iran's revenue streams will constrain its support for Tehran's proxies opposing U.S. interests in the region. According to the State Department, Iran spends roughly $20 billion annually on its military, 4.5% of its gross domestic product, much of it destined for U.S.-designated terror group Hezbollah, fighters in Syria and militants in Yemen.

Iran's crude sales to China fell 21% between May and August, according to Eurasia Group. But it is unclear how long China will stick to that trend.

State-owned oil and natural-gas companies in China, along with Russia and Turkey, account for half of the 19 companies likely to stay in Iran, according to Foundation for the Defense of Democracies, a Washington think tank that supports sanctions. China National Petroleum Corp. is considering buying Total's share of a multibillion-dollar expansion of the South Pars gas field. And Sinopec has signaled it plans to continue buying Iranian crude.

 

The escalating trade war between China and the U.S. could give Beijing reason to either inflame or avoid additional confrontations with Washington. China's role in enforcing North Korea sanctions—critical to U.S. efforts to strongarm Pyongyang into abandoning nuclear weapons—gives the country negotiating leverage.

India, another major Iranian oil importer, is showing signs of compliance.

Executives at private companies that collectively represent half of India's Iranian purchases, said volumes are already down and they will stop importing completely if the U.S. doesn't grant the country a waiver. State companies are signaling they may not renew contracts expiring in March.

Turkey, where some banks were found to have handled large sanction-evasion schemes during the Obama administration, now faces suspicion as a potential source of sanctions leakage. Looming U.S. fines against Turkish financial institutions—penalties that some analysts say could be large enough to break Turkey's brittle financial system—may help avert a repeat of the past.

Anant Vijay Kala and Biman Mukherji contributed to this article.

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THE WALL STREET JOURNAL.

Heard on the Street
Markets
**Michael Kors Is Overpaying for Versace Glamour; The $2.4 billion Michael Kors is reportedly splurging on Versace looks like a bad use of shareholder funds**

By Stephen Wilmot
478 words
24 September 2018
01:03 PM
The Wall Street Journal Online
WSJO
English


Versace fits nicely with Michael Kors's strategy of creating a multibrand, global fashion group. That may be the problem: If you make clear you want a deal, you don't get a good one.

Michael Kors is close to paying €2 billion ($2.4 billion) for Versace, The Wall Street Journal reported Monday. The Italian fashion brand is best known for glamorous, sometimes provocative designs and the tragic assassination of its founder, Gianni Versace, in Miami Beach in 1997.

It would be a move upscale for Michael Kors, a brand known for so-called affordable luxury. The company was a **stock-market** darling for a couple of years after its initial public offering in 2011 as it took market share from established rival Coach. Then Kate Spade became the hot new label and Michael Kors went the way of Coach, prompting a strategic rethink.

Last year Michael Kors bought shoe brand Jimmy Choo for $1.2 billion, and chief executive John Idol talked about more big acquisitions to forge a "global fashion luxury group." His template seemed to be the big Parisian luxury conglomerates LVMH Moët Hennessy Louis Vuitton SE and Gucci-owner Kering, which own more than a dozen brands each and have been growing faster than U.S. competitors. Coach also wants to diversify: Last year the company bought Kate Spade and changed its name to Tapestry to portray itself as a holding company.

Michael Kors is reportedly paying roughly three times sales for Versace, which is barely profitable. Michael Kors stock itself commands just over two times sales. Mr. Idol risks destroying shareholder value by absorbing Versace into a holding company known for affordable luxury, which may be why the shares fell 9% on Monday morning.

Versace has fallen on hard times. In 2014 the family, led by Gianni Versace's sister Donatella, brought in private equity group Blackstone to fund an expansion. Rumors of an IPO have surfaced periodically since, but the company failed to get in the luxury revival that other European brands have experienced since mid-2016, making the IPO pitch awkward. Kering was among the potential buyers that thought Versace was too expensive, according to a Reuters report.

Michael Kors also faces the tough task of reviving Versace at a time when its own revival is fragile. Neil Saunders, managing director of consulting firm GlobalData Retail, says a recent improvement in sales has been driven by "an upswing in U.S. consumer sentiment and spending, rather than because the brand is generating much better traction."

Mr. Idol has his work cut out convincing investors he isn't wasting their money.

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THE WALL STREET JOURNAL.

Markets

**Palladium Rally Leads Sudden Rebound in Metals; The metal, regarded as an indicator for automobile demand, has surged 25% since mid-August**

By Amrith Ramkumar
646 words
24 September 2018
12:51 PM
The Wall Street Journal Online
WSJO
English


A runaway rally in the silvery-white metal palladium is revving up investor optimism for global growth.

Palladium, used in automobile converters that make toxic emissions less harmful, has surged 25% since mid-August on softer-than-expected tariffs from China and the U.S., as well as signals that the Trump administration wants to compromise on trade. Prices are now at their highest level in nearly seven months, with the most-active futures on track to post their ninth straight session of gains Monday—the longest such streak since October 2014, according to Dow Jones Market Data.

Some investors look at palladium as an indicator for car demand and sentiment. Its rapid increase and signs that the Chinese government wants to spur domestic growth have led a rally in other metals markets. On Friday, nickel rose nearly 5% on the London Metal Exchange, and copper surged 4.3% to cap off its best week in nearly two years. Most other metals were roughly flat Monday as traders weighed the latest trade headlines.

Palladium is "a small market, but sometimes these small markets can lead in terms of sentiment," said Tai Wong, head of metals trading at BMO Capital Markets.

Investors look at industrial metals—widely used in manufacturing and construction—broadly to gauge growth world-wide. A monthslong price slide in these markets had eroded investor confidence, pushing money managers into U.S. assets throughout the year.

Yet recently, some analysts appear much more confident that a full-blown trade war and slowdown in China won't materialize. Japan's Nikkei Stock Average just had its best two-week stretch since July 2016, and the Shanghai Composite logged its best week in 30 months. The Stoxx Europe 600 posted its largest one-week advance since March.

Additionally, a sharp climb in new-car registrations in the European Union during July and August boosted palladium prices, Commerzbank analysts said in a recent note to clients.

Investors have grown more optimistic about the outlook for palladium, with hedge funds and other speculative investors increasing net bets on higher prices for the fourth consecutive week through Sept. 18. Unlike with other metals in recent weeks, **bullish** wagers have generally outnumbered **bearish** ones for palladium.

Analysts say the prospect of global demand exceeding supply for a third straight year has also made palladium more attractive than other materials. Johnson Matthey PLC, a London-based metals trader and one of the world's largest makers of catalytic converters, expects steady consumption of palladium for gasoline engines to fuel another supply deficit this year.

Meanwhile, traders say the roughly $200-per-troy-ounce gap between palladium and its close relative platinum, which has historically been more expensive, shows investors' preference for the former. Palladium is used for gasoline-engine cars, while platinum is used more heavily in catalytic converters that go in diesel cars.

Palladium also has benefited from the dollar's weakness, which makes commodities denominated in the U.S. currency cheaper for overseas buyers. The WSJ Dollar Index, which tracks the dollar against a basket of 16 other currencies, fell 0.1% Monday. It has dropped roughly 1.5% since hitting a 15-month high last month.

Despite the recent palladium rally, some traders expect metals prices to remain **volatile** as trade discussions continue and more economic data is released. China scotched trade talks with the U.S. that were planned for the coming days, The Wall Street Journal reported over the weekend.

But a continued metals rally could have investors feeling rosier. "The mood certainly has shifted," Mr. Wong said.

To receive our Markets newsletter every morning in your inbox, click here.

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# THE WALL STREET JOURNAL.

Markets

**Everything Looked Great for the Dollar Recently, So Why Didn't It Go Up? The greenback has been weakening for the past month despite fundamentals; the preceding months hold clues as to why**

By James Mackintosh
759 words
24 September 2018
01:01 PM
The Wall Street Journal Online
WSJO
English


Here's the standard market narrative on the dollar: It is significantly stronger this year because the U.S. economy has been on a tax-cut-fueled bender, the gap between U.S. interest rates and those of other major economies is the biggest in at least a decade, and the rest of the world has failed to live up to hopes for growth. Add in fears about emerging markets, Italian anti-European populism and Brexit, and of course the dollar has been great.

Except it hasn't, at least recently. It has been weakening for the past month, as market sentiment overpowered the fundamentals of economics and interest rates. To get a proper understanding we should look back further; this year the story of the dollar is nuanced, and comes in four chapters.

At the start of the year, the dollar weakened against almost every currency of note as investors became wildly overoptimistic about global growth. In April the dollar turned around as that optimism went into reverse and investors started to bet that the U.S. economy would power ahead of the rest of the world.

By July the dollar had made back all its losses and more, and was contributing to trouble in emerging markets reliant on foreign financing, particularly Argentina and Turkey. At this point fear began to set in: Emerging-markets contagion, Italian populism and the trade war all justified a flight to safety. The dollar accelerated upward, except against even safer havens such as the yen, against which it began to fall again.

The final phase is the most puzzling: From mid-August the dollar ignored all those supportive fundamental factors. The economy remains strong. The extra yield offered by two-year Treasurys over German two-year bonds has widened to 3.35 percentage points, the highest since before the Berlin Wall fell in 1989. The trade fight with China has intensified. Emerging markets, Italy and Brexit remain live issues. And instead of rising, the dollar has fallen against the euro, sterling and yuan, while emerging-market currencies have been much more stable than they were. (Troubled Argentina is a notable exception.)

A clue to what is going on can be found in the yen, the one major currency weaker against the dollar since mid-August. Investor demand for the safety of Japan has waned because global risk appetite has risen. It shows up in the lower—though still high—**volatility** of emerging markets, in the lower—though still high—extra yield on offer from Italian bonds over German bonds, and in the subdued investor response to the latest trade skirmishes.

"We've come through the worst and the market was positioned for bad news," says Simon Derrick, chief currency strategist at Bank of New York Mellon. "Who's left that doesn't know that there's bad news in any of these markets?"

A shift from bracing for disaster to being merely concerned explains a lot of the dollar's recent decline, and raises an intriguing point about the direction of causation. Usually the danger is that a strong dollar will cause an emerging-markets crisis. But fear of a broad emerging-markets crisis also can cause a stronger dollar, as investors flee for safety; the subsequent lack of contagion (so far) from emerging markets can at least help to cause a weaker dollar again.

The rest of the dollar weakness can be explained by China. Many investors thought China would find it hard to stimulate its weakening economy without a repeat of the 2015-16 capital flight that roiled global markets. But last month China managed to end the fall in its currency with little more than words, calming fears that a yuan devaluation might hit the global economy.

There are still a lot of hedge funds betting on a rising dollar, according to Commodity Futures Trading Commission data on futures positions, suggesting plenty of positions to be unwound if global sentiment keeps improving. On the other hand, U.S. short-term fundamentals are looking great for the dollar, with domestic economic data less disappointing than it had been, and more disappointing in Europe. That ever widening gap in yields in favor of the greenback should make dollars attractive, too. Fundamentals are likely to reassert themselves eventually, but sentiment has the momentum for now.

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The New York Times

Fact Check of the Day
U.S.; Politics
**Trump's Inaccurate Claim That U.S. Is 'the Fastest-Growing Economy in the World'**

By Linda Qiu
320 words
24 September 2018
07:18 PM
NYTimes.com Feed
NYTFEED
English


— President Trump, in remarks at the United Nations General Assembly meeting on Monday

The United States does have one of the fastest growing of the world's largest economies. But it is not the fastest growing in the whole world.

The Organization for Economic Cooperation and Development compiles quarterly growth in real gross domestic product for its 36 member nations and nine other major economies like China, India and Brazil. The United States had the eighth-highest rate in the second quarter of 2018 out of this group. Its rate was the highest among the Group of 7, the largest of the industrialized democracies.

Among the entire world, however, the United States is nowhere near "the fastest-growing economy." Growth rates among developing nations, while **volatile**, often exceed those of the big industrialized countries. In 2017, the United States' G.D.P. annual growth rate ranked in the bottom third out of more than 180 countries, according to data from the World Bank.

The International Monetary Fund's projections for G.D.P. growth rate for 2018 place the United States among the bottom half of about 190 countries. Similarly, Harvard University's Atlas of Economic Complexity projects that the United States will reach an annual growth rate of 3.07 percent by 2026, placing it No. 104 out of 121 countries.

The president may have been referring to the soaring **stock market** with his $10 trillion figure, as he has donein the past, but the **stock market** is not the economy, though they can influence each other. If the economy did grow by $10 trillion, it would have grown by more than 50 percent; in reality, G.D.P. rose by about $1.3 trillion from the first quarter of 2017 to the second quarter of 2018.

Document NYTFEED020180924ee9o008y9

The New York Times

Business Day; DealBook
**Buybacks Continued to Boom Last Quarter: DealBook's Closing Bell**

By Stephen Grocer
627 words
24 September 2018
07:15 PM
NYTimes.com Feed
NYTFEED
English


Get the DealBook newsletter to make sense of major business and policy headlines — and the power-brokers who shape them.__________

The pace at which companies are repurchasing their shares is gaining momentum. Companies in the **Standard & Poor's 500**-**stockindex** bought back a record $189.1 billion of their shares during the second quarter, up nearly 60 percent from a year ago, according to S.&P. Dow Jones Indices. The figure topped the previous high of $178 billion set during the first quarter. Through the first six months, corporate buybacks stand at $379.7 billion, a 50 percent increase from the same period in 2017. Technology companies were the busiest, accounting for nearly $37.5 percent of the activity.

Apple again led the way. The iPhone maker bought $21.9 billion of its shares back last quarter. Apple accounted for 11.5 percent of all buyback activity by **S**.**& P**. **500** companies.

Rates are rising, but that may not mean a **bear market** is around the corner. The Federal Reserve meets this week and is widely expected to raise rates for the third time this year. Among the biggest concerns of investors is whether the Fed would eventually push too far with its tightening and end the nearly decade-long **bull market**. Sam Stovall, chief investment strategist of CFRA, does not believe that a rise in interest rates in the near term will cause a **bear market** in stocks. In his analysis, he looked at the difference between the Fed funds rate and the yearly change in the Consumer Price Index. In the lead up to every bear markets since 1955, the Fed funds rate was, on average, 2.5 percentage points higher than the yearly change in inflation. Now, though, the target range for the Fed funds rate is below the change in inflation and will remain so even if the Fed raises rates this week, Mr. Stovall notes.

But can the Fed even slow the economy when the private sector is so strong? Ian Shepherdson, the chief economist at Pantheon Macroeconomics, explained that recessions in developed economies were caused by the unwinding of imbalances in the private sector — for instance, the level of debt held by households ahead of the financial crisis — set off by central bank tightening. Now, the level of debt held by households or corporations is not concerning. "The only domestic imbalance in the economy right now is in the public sector," writes Mr. Shepherdson. That means the Fed does not need to take drastic actions. That could change by the middle of 2019, when continued strength in the labor market and growing wages, along with the effects of the tax cuts could force the Fed to move faster than expected.

The price Brent crude oil climbs above $80 a barrel, its highest level since 2014. The move follows the weekend decision by members of the Organization of the Petroleum Exporting Countries and other major producers like Russia to hold prices production steady. Brent is now up roughly 25 percent this year, and some forecasters expect it to rise to $90. But could **oil prices** surge and crash as they did in 2008? Analysts at Bank of America Merrill Lynch said that possibility had increased.

How long will it take Americans to forgive the financial crisis bailouts? Twenty-five years, according to Jamie Dimon, the chief executive of JPMorgan Chase. Speaking at an event sponsored by the World Affairs Council in Philadelphia, Mr. Dimon said the government did the right thing, Bloomberg reports.

Apple accounted for 11 percent of all buyback activity by **S**.**& P**. **500** companies during the second quarter. | CHINATOPIX, via Associated Press

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THE WALL STREET JOURNAL.

Markets

**Bitcoin ETFs Keep Trying, Despite Regulators' Rejections; SEC has said no at least 10 times, but firms want to be ready in case it changes its mind**

By Asjylyn Loder
1,050 words
23 September 2018
10:05 PM
The Wall Street Journal Online
WSJO
English


Bitcoin enthusiasts trying to launch funds that would bring the cryptocurrency to small investors have been rebuffed at least 10 times by Wall Street's top regulator.

That hasn't stopped them. There's at least one application for a bitcoin exchange-traded fund still pending with the Securities and Exchange Commission, and more are planned, like one from cryptocurrency asset manager Bitwise Asset Management.

First advantage

Why keep pushing? History shows that the first fund to market has a huge advantage over later entrants, so firms are jockeying to keep their place in line in case regulators change their minds.

There is, of course, no shortage of opinions about what the SEC should do and what it will do. One central question concerns the basis of any SEC decision on cryptocurrency ETFs: Does the commission need to determine that cryptocurrencies are a worthwhile investment for individual investors, or should it be enough for fund firms to provide clear warnings about the risks?

"Is [the SEC] a merit regulator, or should investors be able to decide for themselves what to invest in?" says Paul Atkins, a former SEC commissioner and now chief executive of Patomak Global Partners, a financial consulting firm. Resolving that debate will take time, he says.

Will Rhind, founder and chief executive of GraniteShares Inc., one of the aspiring bitcoin ETF firms denied recently, says the commission is being tougher on cryptocurrencies than it has been on other asset classes.

Bitcoin is a virtual currency introduced 10 years ago as an alternative to government-issued money. Last year's rally in bitcoin prices drew throngs of new investors, but prices tumbled by more than half this year, raising concerns about the **volatility** and potential manipulation of the opaque market. Mr. Rhind says that trading in physical markets for oil or gold is also largely unregulated, but that hasn't prevented the SEC from approving ETFs based on those commodities.

"That risk has always been a disclosure issue," Mr. Rhind says. "But in this case, we had to go way beyond that and prove that the market is not being manipulated, which is a standard that is impossible to prove."

The stakes are considerable. The $28.6 billion SPDR Gold Trust, the first (and still largest) ETF backed by gold bars, generates more than $100 million a year in investor fees.

Bitcoin is just the latest example of the $3.7 trillion U.S. ETF industry trying to bring an esoteric asset into the investing mainstream. For all the credit ETFs get for bringing low-cost index funds to the masses, the industry has also made betting on high-risk strategies as easy as buying blue-chip stocks.

For example, ETFs have popularized speculation on commodity futures and on derivatives tied to **stock-market volatility**, and some employ leverage to double or even triple gains and losses. But investors haven't always understood the risks, and unexpected losses in some funds have led to Congressional hearings, lawsuits and multimillion-dollar fines.

Those controversies may explain some of the SEC's caution when it comes to bitcoin. Also, Jay Clayton, the regulator's chairman, has expressed skepticism about initial coin offerings, saying retail investors are particularly at risk in the once-hot market.

This month, the SEC temporarily suspended trading of two Stockholm-listed cryptocurrency exchange-traded products that had begun trading in U.S. over-the-counter markets.

The latest setbacks for ETF firms include three rejections in August and July's unsuccessful appeal by Cameron and Tyler Winklevoss of an earlier SEC rejection. The Winklevoss twins first applied to launch a bitcoin ETF back in 2013. Their ETF would have backed investors' cash with virtual stockpiles of the digital currency, akin to the way the SPDR Gold Trust is backed by vaults filled with stacks of gold bars.

The SEC wasn't convinced. The commission rejected the Winklevoss proposal in March 2017, in part because of the difficulty of detecting manipulation in the largely unregulated markets where most bitcoin is traded.

Rekindled Fervor

But bitcoin ETF fervor was rekindled late last year after exchange firms CME Group Inc. and Cboe Global Markets Inc. launched bitcoin futures contracts. Fund firms such as First Trust, Direxion, ProShares and GraniteShares proposed ETFs that would invest in the nascent futures market instead of digital stockpiles of cryptocurrency. The hope was that a regulated bitcoin futures market would allay the SEC's concerns.

ETF firms still see a glimmer of hope. At the behest of at least one commissioner, the SEC is reconsidering the three proposals that were turned down in August. The rejections hinged, in part, on a concern that the cryptocurrency futures markets are still too small. It's a problem time may solve, if trading catches on.

History is not necessarily encouraging: The first ETF pegged to **volatility** futures launched five years after the debut of the futures, and the first oil ETF followed oil futures by 23 years.

For all the fuss, a bitcoin ETF is a bigger deal for bitcoin than it is for ETFs. It would lend legitimacy to a market that's still on the margins of high finance. Wrapping cryptocurrency in an ETF could alleviate concerns about fraud, hacking and lost account keys that have made some would-be investors wary. Instead of creating a new account on one of the many bitcoin trading venues, investors could buy the ETF through their existing investment accounts.

"It's an access vehicle," says Elisabeth Kashner, director of ETF research at FactSet. "ETFs have taken certain trading tools and securities and made them more accessible to anyone with a couple hundred bucks and a brokerage account."

Ms. Loder is a Wall Street Journal reporter in New York. She can be reached at asjylyn.loder@wsj.com. Dave Michaels contributed to this article.

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**Bond Yields Approach Highest in 7 Years As Investors Add Risk**

By Daniel Kruger
682 words
24 September 2018
The Wall Street Journal
J
B9
English


The yield on the benchmark 10-year U.S. Treasury note has climbed back to near a seven-year high, a sign of increased optimism that trade disputes and problems in emerging markets won't derail the global economy.

Encouraged by data showing robust U.S. growth, rising wages, gains in corporate profits and persistently low unemployment, investors have pushed stocks to records and ramped up their selling of government debt.

At the same time, forces that had weighed on bond yields, such as worries about tariff fights and turmoil in countries including Argentina and Turkey, have eased.

That leaves investors grappling with a tension between the economic strength that seems primed to push stocks and other riskier assets higher and concerns that those gains could be derailed by anything from the fight over global trade to tightening monetary policy. The Federal Reserve is expected to raise interest rates this week for the third time this year, with investors watching officials' forecast for 2021, seeking clues as to how long policy makers think the expansion can continue.

Rising Treasury yields serve as a reference rate for lending throughout the economy, influencing borrowing costs for homes and cars, or the price of debt for credit-card holders and businesses. Many analysts say a sustained climb above 3% in the 10-year yield would mark the latest sign of the economy's gradual postcrisis strengthening after years of ultralow rates.

"The wall of fear that we were talking about just two weeks ago -- be it Italy or trade wars or emerging markets -- it seems like it's completely collapsed," said Priya Misra, head of global rates strategy at TD Securities. However, it is "not clear to me that any of these risks have fundamentally been solved," she added.

The yield on the **10**-**year Treasury** note, which rises as **bond prices** fall, climbed as high as 3.10% in intraday trading last week, up from 2.85% at the start of September and near its 2018 closing high of 3.11% reached May 17. It is approaching its highest level since July 2011.

One sign the climb in yields is based on investors' increased appetite for risk can be seen in the stability of market-based inflation expectations. Because inflation poses a threat to government bonds by eroding the purchasing power of their fixed payments, rising inflation expectations often accompany climbing yields. Yet one measure of those expectations, known as the 10-year break-even rate, indicates investors lately see the annual rise in the consumer-price index for the next 10 years at a relatively steady 2.1 percentage points.

While yields are rising, they remain low by historical standards, bolstering many analysts' view that the economy can withstand modest near-term increases in borrowing costs.

At the same time, investor confidence has climbed while **volatility** has eased. Stock gains have bolstered the portfolios of higher-income people, while the tightening labor market and rising wages have made people in lower-income groups more optimistic, said Ellen Zentner, chief economist at Morgan Stanley. The **Dow Jones Industrial Average** closed at a record on Friday.

Investors also are less worried that rising bond yields could provoke declines in stock prices than they were earlier in the year. In February, stocks tumbled after the **10**-**year Treasury** yield reached 2.85%, prompting concerns that rising borrowing costs could derail the expansion. Strong economic growth has moderated the risk that higher yields will undermine stocks, several analysts said.

The yield on the two-year note, which typically moves in line with expectations for monetary policy, has climbed faster than the 10-year yield in 2018. That reflects a narrowing dispersion between shorter- and longer-term rates, known as a flattening yield curve. Many view a flattening yield curve as a cautionary signal, as recessions have followed each time short-term rates have exceeded long-term yields since 1975.

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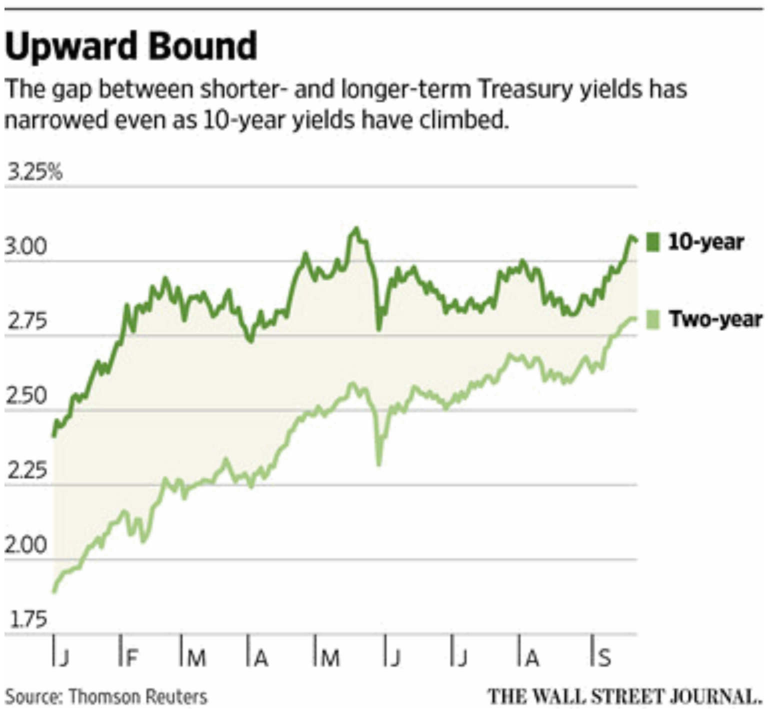
Sam Goldfarb contributed to this article.

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**Buybacks Dress Up Profits --- Tax changes spur stock repurchases as companies move to lift per-share earnings**

By Michael Rapoport and Theo Francis
750 words
24 September 2018
The Wall Street Journal
J
B9
English


Last December's tax overhaul is boosting corporate profits in more ways than one.

The legislation lowered companies' tax bills, improving their earnings. But the change has also helped them fund record stock buybacks -- a move that makes their results appear even better by boosting the per-share earnings they highlight for investors.

**S&P 500** companies bought back a record $189 billion of their own shares in the first quarter, and a similar number -- if not more -- is expected for the second quarter, according to S&P Dow Jones Indices. By contrast, **S&P 500** buybacks totaled no more than $137 billion in any of the six quarters before the tax overhaul.

Stock buybacks make profits appear better by boosting per-share earnings, a metric investors frequently use to justify a company's **stock price**. Buybacks reduce a company's share count, spreading the profits across fewer shares. As a result, companies can report a bigger percentage increase in per-share earnings than the profit results alone may show.

Among the more aggressive companies in buying back stock, Apple Inc. repurchased 112.8 million shares in the quarter that ended in June, contributing 5 cents to its earnings of $2.34 a share. Union Pacific Corp. repurchased about 4% of its shares in the second quarter, helping earnings per share climb substantially faster than net income. Thanks to buybacks, Southwest Airlines Co.'s quarterly per-share earnings rose even though its profit fell from a year earlier.

For the **S&P 500**, per-share earnings in the second quarter rose about 25% from a year ago -- a full 2 percentage points faster than net income, according to data from Thomson Reuters. "It would be fair to assume it is all from buybacks," said David Aurelio, senior research analyst at Thomson Reuters.

The higher per-share earnings have helped lead investors to pay more for stocks. The **S&P 500 index** is posting records after gaining about 10% this year.

"Investors need to realize what they're paying a premium for," said Howard Silverblatt, senior index analyst at S&P Dow Jones Indices.

In all, dozens of large companies bought back 4% or more of their shares outstanding in the 12 months ended in June, according to data from S&P Dow Jones Indices. The resulting boosts to earnings might seem small in any given quarter, but they add up -- Apple's buybacks also added 8 cents a share in the March quarter, for instance. And companies also have started big new buyback programs, suggesting earnings-per-share increases will continue.

The buybacks aren't necessarily done for the express purpose of increasing per-share earnings. Many companies say they want to return excess capital to shareholders. Others intend to offset new shares issued to employees as compensation.

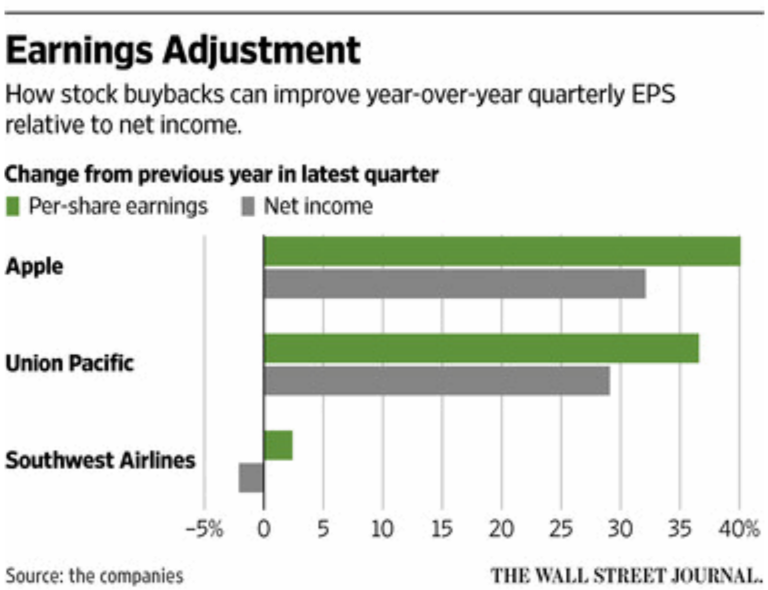
The per-share earnings increases generated by stock buybacks are low quality, inflating results without underlying substance, said Gregory Milano, chief executive of Fortuna Advisors, a financial consulting firm that has examined buyback trends. "It has less value."

Companies play down the buyback effect. They say their earnings are strong even without buybacks, and that while the buybacks add to per-share earnings, the effect is clear to investors and baked into the analyst earnings estimates that drive stock prices.

Apple pointed to its past statements that its earnings growth is accelerating and that tax overhaul "enables us to deploy our global cash more efficiently," leading it to put forward plans to create 20,000 U.S. jobs and invest $350 billion in U.S. operations over the next five years.

Union Pacific's buybacks contributed 9 cents to its second-quarter per-share earnings, helping that metric to climb 37%, while net income rose 29% from a year ago. The railroad's finance chief, Robert Knight, said the buybacks "represent the return of excess cash to our shareholders and are consistent with guidance we provided to the financial-analyst community."

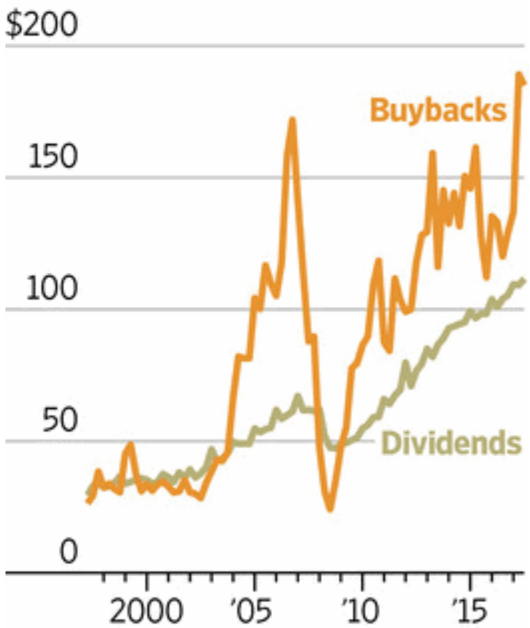
Southwest Airlines' second-quarter net income excluding items declined 2.1% from a year ago. On a per-share basis, however, it rose 2.4%, in part because the company has repurchased 28.3 million shares in the past year. Southwest said its per-share earnings growth "has been driven primarily by the strong financial performance of our robust network."



## Capital Returns

Quarterly dividend and buyback spending for S&P 500 companies




Note: 2Q 2018 buyback figure is preliminary.
Source: S&P Dow Jones Indices
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**OPEC Predicts U.S. Shale Oil Will Peak Late Next Decade**

By Christopher Alessi
528 words
24 September 2018
The Wall Street Journal
J
B2
English


ALGIERS -- U.S. shale-oil production will peak by the late 2020s, triggering renewed demand for OPEC crude after an expected decline and stagnation, the oil cartel said Sunday.

In its latest forecast on the global oil landscape, the Organization of the Petroleum Exporting Countries said it expects U.S. shale growth to "slow significantly" after 2023, before peaking at 14.3 million barrels a day between 2027 and 2028. Output should then fall to an average of 12.1 million barrels a day by 2040, according to OPEC.

The use of hydraulic fracturing in the U.S. to drill for oil in shale rock -- known as fracking -- has dramatically reshaped the face of the global oil industry over the past decade, rivaling OPEC for market share. Shale was largely behind a glut of American oil that flooded the market over four years ago, leading **oil prices** to fall to $30 a barrel from more than a $100 a barrel in late 2014.

In 2018, U.S. shale production is growing at a faster pace than it did during the boom years of 2011 to 2014, the International Energy Agency said earlier this year. The IEA has forecast that U.S. shale-oil production will plateau in the late 2020s, while total non-OPEC production should decline.

OPEC projects that "the strongest annual increases are seen in the near term, in which total U.S. tight oil increases by an average of 1.4 million barrels a day" annually from this year to 2020.

The world's appetite for OPEC crude, meanwhile, should fall to 31.6 million barrels a day in 2023, compared with 32.6 million barrels a day in 2017, before again rising to current levels when U.S. shale supply peaks, the cartel said.

"Thereafter, a gradual decline in non-OPEC liquids supply, coupled with moderate, but sustained global demand growth, leads to a steady increase in demand for OPEC crude, which rises to nearly 40 million barrels a day by 2040," the OPEC report noted.

OPEC's updated outlook comes as the oil cartel is meeting in Algiers with its partner producers, including Russia. The discussion centers on whether producers should raise crude production levels and supply more oil to global markets, amid continued pressure from President Trump to rein in rising prices.

More broadly, OPEC on Sunday also said it expects global demand for oil to increase by an average of 1.2 million barrels a day in the medium term, reaching 104.5 million barrels a day by 2023. But the cartel said it expects growth to "decelerate over time," reaching 111.7 million barrels a day in 2040. That is up from its forecast last year for 2040 of demand of roughly 107.5 million barrels a day.

The cartel has said it doesn't expect global demand for oil to peak before 2040. That is largely in line with the forecast of the International Energy Agency, which has argued that global oil demand will grow slowly past 2040.



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**Innovations In Finance (A Special Report) --- Policy Makers Rethink 2% Inflation: That number has long been the Holy Grail for central banks. The big debate now is over what would be a better target.**

By Tom Fairless
1,085 words
24 September 2018
The Wall Street Journal
J
R7
English


What's so special about 2% inflation?

From Ottawa to Oslo, policy makers have been considering whether that level of consumer-price growth, a Holy Grail for the world's major central banks over the past quarter-century, is still relevant.

The 2% target was always an arbitrary figure, some economists argue, and even if it was optimal two decades ago, that is no longer the case given deep changes that have since reshaped the global economy.

Trouble is, it isn't clear what inflation rate would be better. Dozens of academic studies that considered that question have produced answers ranging from 6% to less than zero, according to a survey published last year by Federal Reserve economist Anthony M. Diercks. While deflation, or steadily falling prices, are generally considered to weigh on economic growth, a mildly negative inflation rate would also have benefits, such as eliminating the cost of holding cash.

The debate has gained traction since former Federal Reserve Chairwoman Janet Yellen suggested last year that the U.S. central bank might revisit its 2% inflation target. Canadian officials have also suggested they might be open to changing the Bank of Canada's 2% target when its mandate comes up for review in 2021.

Recently, economists have tended to call for a higher target. The main argument: That would give central banks more room to fight economic downturns because higher inflation implies higher interest rates, thus giving the Fed more room to cut.

"Whatever [inflation] rate was thought to be optimal in 2006 or before is now too low," says Olivier Blanchard, a senior fellow at the Peterson Institute for International Economics in Washington, D.C., who has called for a 4% target.

Factors such as aging populations, low economic growth and higher savings rates are working to push down the neutral interest rate, at which the economy is growing at a sustainable rate for the long run and inflation is stable. As a result, central banks run a greater risk of taking benchmark interest rates to zero or below when seeking to support growth.

And yet, Norway's government said recently it would reduce its central bank's inflation target, to 2% from 2.5%, arguing there was no longer any reason to diverge from international norms. With inflation near target, the central bank raised interest rates to 0.75% on Sept. 20.

The case for a higher target runs like this: Policy makers find it difficult to cut benchmark interest rates much below zero. If inflation is 2%, that means central banks can reduce the real interest rate -- the benchmark rate minus inflation -- to minus 2% by cutting the benchmark rate to zero. If inflation were higher, say 4%, cutting the benchmark rate to zero would push the inflation-adjusted rate to minus 4%, providing an extra kick for the economy.

Higher inflation could have other benefits. It could help economies adjust after a downturn by lessening the need for outright wage cuts, because rising prices will erode wages anyway. It could also make it easier for borrowers to pay down debt, though that is something that lenders historically have always resisted. A 2009 study estimated that U.S. inflation of 6% for four years could reduce the nation's debt-to-GDP ratio by around 20 percentage points, similar to what happened after World War II.

Other economists have cast doubt on whether that level of inflation would reduce the debt ratio by so much. And many worry that central banks would struggle to push inflation to 6% anytime soon, given how hard it was to hit 2%.

Vitor Constancio, the European Central Bank's vice president back in May, said at the time that while he had "no theoretical objections" to a "mild" upward revision of the inflation target, moving to a new target could undermine central banks' hard-won credibility.

The ECB is among a group of central banks to have cut benchmark interest rates below zero, a novel move aimed at providing extra stimulus to their economies. Former Fed Chair Ben Bernanke has suggested that negative rates might be a better alternative to higher inflation targets.

"Yes, negative interest rates raise a variety of practical problems, as well as political and communications issues, but so does a higher inflation target," Mr. Bernanke wrote in a 2016 blog post. "In the political sphere, the fact that negative rates would be temporary and deployed only during severely adverse economic conditions would be an advantage."

Higher inflation can have drawbacks, as many economies have learned through painful experience. It could distort the tax system and mask economic signals, such as whether goods are rising in price because they are scarce. Banks might demand an inflation-risk premium when granting long-term loans, because high inflation can lead to more **volatile** price movements, says Michael Schubert, an economist with Commerzbank in Frankfurt. Thus, financing would become more expensive, causing companies to invest less.

Crucially, an inflation rate of 2% allows households and businesses to largely disregard price increases. That effect might be lost if inflation is allowed to rise much higher.

"We know that some number higher than a 2% to 3% rate of inflation will materially enter decision-making, because we have had plenty of experience of higher rates of inflation that demonstrates that," says Guy Debelle, deputy governor of Australia's central bank. "How much higher though, we don't really exactly know."

One possible solution: Central banks could allow inflation to rise a bit above 2% without aggressively trying to bring it down. That could give them more room for maneuver, and gradually inflate away some of the world's enormous debt load.

It seems to already be happening in the U.S., where inflation in August was 2.7%.

Although eurozone inflation has accelerated in recent months and is now 2%, the ECB has signaled that it won't raise rates for about a year.

Joseph Gagnon, a fellow at the Peterson Institute, says the Fed "ought to tilt policy toward overshooting, not for its own sake, but to avoid" undershooting its target again in future.

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**Innovations In Finance (A Special Report) --- The Bitcoin Push: Bitcoin ETFs keep trying, despite SEC rejections**

By Asjylyn Loder
725 words
24 September 2018
The Wall Street Journal
J
R5
English


Bitcoin enthusiasts trying to launch funds that would bring the cryptocurrency to small investors have been rebuffed at least 10 times by Wall Street's top regulator.

That hasn't stopped them. There's at least one application for a bitcoin exchange-traded fund still pending with the Securities and Exchange Commission, and more are planned, like one from cryptocurrency asset manager Bitwise Asset Management.

Why keep pushing? History shows that the first fund to market has a huge advantage over later entrants, so firms are jockeying to keep their place in line in case regulators change their minds.

There is, of course, no shortage of opinions about what the SEC should do and what it will do. One central question concerns the basis of any SEC decision on cryptocurrency ETFs: Does the commission need to determine that cryptocurrencies are a worthwhile investment for individual investors, or should it be enough for fund firms to provide clear warnings about the risks?

"Is [the SEC] a merit regulator, or should investors be able to decide for themselves what to invest in?" says Paul Atkins, a former SEC commissioner and now chief executive of Patomak Global Partners, a financial consulting firm. Resolving that debate will take time, he says.

Will Rhind, founder and chief executive of GraniteShares Inc., one of the aspiring bitcoin ETF firms denied recently, says the commission is being tougher on cryptocurrencies than it has been on other asset classes.

Bitcoin is a virtual currency introduced 10 years ago as an alternative to government-issued money. Last year's rally drew throngs of new investors, but prices tumbled by more than half this year, raising concerns about the **volatility** and potential manipulation of the opaque market. Mr. Rhind says that trading in physical markets for oil or gold is also largely unregulated, but that hasn't prevented the SEC from approving ETFs based on those commodities.

"That risk has always been a disclosure issue," Mr. Rhind says. "But in this case, we had to go way beyond that and prove that the market is not being manipulated, which is a standard that is impossible to prove."

Bitcoin is just the latest example of the $3.7 trillion U.S. ETF industry trying to bring an esoteric asset into the investing mainstream.

For example, ETFs have popularized speculation on commodity futures and on derivatives tied to **stock-market volatility**, and some employ leverage to double or even triple gains and losses. But investors haven't always understood the risks, and unexpected losses in some funds have led to Congressional hearings, lawsuits and multimillion-dollar fines.

Those controversies may explain some of the SEC's caution when it comes to bitcoin. Also, Jay Clayton, the regulator's chairman, has expressed skepticism about initial coin offerings, saying retail investors are particularly at risk in the once-hot market.

The latest setbacks for ETF firms include three rejections in August and July's unsuccessful appeal by Cameron and Tyler Winklevoss of an earlier SEC rejection. Their ETF would have backed investors' cash with virtual stockpiles of the digital currency.

The SEC wasn't convinced. The commission rejected the Winklevoss proposal in March 2017, in part because of the difficulty of detecting manipulation in the largely unregulated markets where most bitcoin is traded.

But bitcoin ETF fervor was rekindled late last year after exchange firms CME Group Inc. and Cboe Global Markets Inc. launched bitcoin futures contracts.

Fund firms such as First Trust, Direxion, ProShares and GraniteShares proposed ETFs that would invest in the nascent futures market instead of digital stockpiles of cryptocurrency. The hope was that a regulated bitcoin futures market would allay the SEC's concerns.

ETF firms still see a glimmer of hope. At the behest of at least one commissioner, the SEC is reconsidering the three proposals that were turned down in August. The rejections hinged, in part, on a concern that the cryptocurrency futures markets are still too small. It's a problem time may solve, if trading catches on.

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THE WALL STREET JOURNAL.

Markets

**Struggling U.S. Farmers Worry About a Resurgent Russia; Russian wheat exports are booming despite a crushing price slump, as the country's farmers finally emerge from decades of neglect**

By James Marson
1,949 words
23 September 2018
12:22 PM
The Wall Street Journal Online
WSJO
English


Corrections & Amplifications

In September, oil prices were down about 30% from their high in 2014, after recovering from a swoon of about 77%. An earlier version of this article incorrectly stated that oil prices at the time were down 25% from their high in 2014, after recovering from a swoon of more than 60%. (Nov. 20, 2018)

OTRADNAYA, Russia—Vladimir Mishurov transformed the remnants of the "Lenin's Path" collective farm in this village into a profitable business. He also helped make Russia the world's largest wheat exporter for the first time since the last years of the czars.

Over the past decade or so, Mr. Mishurov replaced his aging Russian equipment with a dozen high-tech machines from John Deere and other makers, and started using powerful new fertilizers and seeds. He bought and rented more acres from neighbors and family, eventually reaching about 3,600, taking advantage of Russia's overall low prices for land.

And as many farmers do in the U.S., he often worked days on end with little sleep, especially during the harvest.

The major difference between Mr. Mishurov and a farmer on America's Great Plains: The Russian's costs are lower, and mostly in rubles, making his overseas sales—priced in dollars—immensely more valuable.

Amid a multiyear, brutal slump in grain prices, Russian agriculture is thriving. The country exported more than 40 million tons of wheat in the year ending June, around 50% more than the previous year, and the highest level for any country in the past quarter-century. Russia overtook the U.S. as the world's biggest exporter of wheat in 2016, and again beat the U.S. in 2018.

The growing Russian competition is one more pressure point threatening American farming, which is facing the biggest wave of farm closures in the U.S. since the 1980s. A global oversupply of grain has pushed prices down to around half the level in 2012, when prices peaked, making it difficult to turn a profit in dollars.

U.S. trade disputes with China and other countries could make Russian wheat even more attractive, if big buyers apply retaliatory tariffs to U.S. grains. China has added a 25% tariff on U.S. wheat, but Chinese restrictions on imports from Russia have prevented Moscow from taking advantage yet, according to Swithun Still, director at Switzerland-based Solaris Commodities SA, which trades Russian grain.

For now, "it's not the trade war, it's economics" that is helping Russian wheat compete, even in places close to the U.S. such as Mexico, Mr. Still said. Russian "quality got better, and it's cheaper."

Russian farmers come out ahead when export earnings are converted into rubles. Since the Russian currency has depreciated, a dollar now converts to twice as many rubles as it did in 2014. Russia has a similar advantage against the euro and other currencies. Russian farmers can cover their costs at home to keep planting, and also undercut Western competitors on price.

Russia's surge of agriculture exports, including grains, fish and meat, is part of an effort to diversify the economy away from crude oil. Oil and natural gas were once the source of half of federal budget revenues. With oil prices still down 30% from their high in 2014—recovering from a swoon of about 77%—exports now account for around 40% of budget revenues.

"Given the fall in prices for oil, grain has come to the fore. Grain is our oil," then-Agriculture Minister Aleksandr Tkachev said in 2016.

Less-expensive Russian wheat is pushing U.S. and European grain out of import-dependent countries in the Mideast and North Africa, where the Kremlin has made a military and diplomatic push for influence in recent years.

Agriculture exports, at $20.7 billion in 2017, have overtaken the arms industry as Russia's No. 2 earner. Wheat makes up about a quarter of the total.

Russia harvested an area of wheat almost twice as large as the U.S. in the year ended in June, according to the U.S. Department of Agriculture. American farmers, seeing little opportunity to profit, planted the smallest area of wheat since records began a century ago. U.S. wheat production shrank 25% in the year.

Mr. Mishurov's farm is on the fertile steppe of southern Russia. The area is the country's biggest grain producer—a bread basket known for its mineral-rich black earth and mild climate.

Now 46 years old, he spent his late teens and early 20s driving a bone-rattling tractor that needed its motor refurbished every year and left his hands callused. A lack of cash meant workers were paid in sacks of flour, wheat or sugar, and drunkenness was pervasive.

At the start of the 20th century, Russia had been the world's largest exporter of wheat. The Soviets killed and imprisoned millions, including many of the most-successful farmers, as part of an effort to install a system of collective farming that proved inefficient. By the 1970s, the Soviet Union had to import grain.

Collective farms stumbled on after the Soviet Union collapsed in 1991, often still managed by the same bosses without business smarts or cash to invest.

"No one was in charge," said Mr. Mishurov. "They couldn't adapt to the market economy. They were accustomed to unthinkingly following instructions."

Farmhands worked "to pass the time of day until they could go home," said Andrei Burdin, a farmer from a nearby village who works land that was once part of the "Dawn of Communism" collective farm. "Farming was at a dead end."

Russia opened the land market at the end of the 1990s, but new investors and their managers tended to be far from the land and averse to risks, farmers said.

Mr. Mishurov, who worked as chief agronomist at a large farming conglomerate, recalled telling an executive in the early 2000s that using pesticide could increase the barley crop by around a quarter.

" 'No, Vova, it's enough already,' " he said the executive replied, using a nickname. "Why should I persuade someone to earn more money?" Mr. Mishurov said.

He struck out on his own in the mid-2000s. At first, he pooled land with relatives and used whatever equipment he could lay his hands on. Today, he grows wheat, barley, beets, corn, sunflowers, peas and other crops.

Mr. Burdin, 43, started farming around 250 acres in 2005 with a dilapidated tractor and planter. He invested early profits into more-efficient vehicles and better fertilizer, and expanded territory by renting from neighbors.

"When we made the first money, I didn't buy a Mercedes or an apartment," he said. "I put it into the next season."

At first, he bought Russian equipment, but later upgraded to John Deere tractors and combines, which the Russians call zelyonaya tekhnika, or "green machines." Mr. Burdin said he tested a John Deere combine against a Russian one and found it produced about one-third more grain from the same area.

He also added a planter from Sweden's Vaderstad AB that shoots seeds into the ground at the optimal depth and intervals, improving yields. He now farms about 3,700 acres.

In April, while loading the planter with seed, Mr. Burdin joked with farmhands about equipment in the old days. He recalled working with a pesticide sprayer that would soak him with chemicals. He said he could only work for about four hours at a time before giving up, out of fear for his health. Now, his sprayer can measure how much pesticide to spray and where, keeping costs down.

 

The price of land in the region where Messrs. Mishurov and Burdin live is significantly lower than for many foreign rivals. On average, farmland in Romania, a European Union member on the Black Sea, is nearly three times the price, while farmland in Iowa and Kansas is more than five times the price, according to a 2017 survey by Moscow-based SovEcon, which provides consulting services, analysis and forecasts on Russian agriculture.

Mr. Burdin said Russian seeds and fertilizers still cost less than Western brands, even though they have improved significantly in recent years. He buys wheat seeds from a state-run agricultural institute, and can plant the seeds produced from those plants the next season. Many American farmers use expensive, high-yield, patented seeds from companies such as Bayer AG or DowDuPont Inc., which don't allow the produced seeds to be planted, requiring farmers to buy fresh seeds annually.

Transport costs are also low for the region. It is close to Black Sea ports, and gasoline costs are much lower than in Western Europe. Mr. Burdin and Mr. Mishurov run their own fleets of trucks that move grain to the Novorossiysk port some 200 miles away by road.

Private and state-owned companies have modernized grain terminals in recent years and increased their capacities. Farmers can use an app on a smartphone to book a slot for their trucks to deliver grain, rather than the old system of having trucks wait in line for days.

Bumper harvests are stretching infrastructure. Windows for unloading grain are snapped up quickly, and farmers are often assigned slots several days after a requested time, Mr. Burdin said.

Exports "could be even higher if they could figure out how to load more," he said.

Russia has made it a priority. President Vladimir Putin ordered officials to tackle infrastructure bottlenecks that are holding back exports. In inland areas, large distances and a lack of train cars and storage silos hamper grain from reaching external markets.

One of Russia's largest terminals in Novorossiysk is completing a three-year modernization this year that will nearly double its capacity. Other companies have announced plans to build or expand terminals on the Black Sea, the Baltic Sea in the north and in the Far East. Officials said expansions at ports could increase export capacity of grains by 50% to 7.5 million tons a month by 2020.

Government officials tout the importance of state subsidies, including inexpensive loans to help farmers replace old equipment. Analysts and farmers say the state's efforts to support agriculture have been hit and miss. Subsidies often make their way to well-connected companies, investment in infrastructure has been slow and bureaucrats and other officials often expect bribes.

"Farmers received the freedom to do business in the way they thought most efficient," said Andrei Sizov Jr., managing director of SovEcon. "The role of the state was quite muted in the last 10 years, and that was good for the industry."

Giant agroholdings, conglomerates often created by wealthy tycoons or people close to top federal and regional government officials, have built up spreads that dwarf Western farms. Individual farms larger than 250,000 acres, or nearly 400 square miles, account for around 13% of all land farmed in Russia, according to Mr. Sizov.

Mr. Mishurov can now afford to collect and restore a half-dozen vintage Soviet cars and vacation in the Maldives and Thailand, although he said he prefers staying home.

The poor villages here depend on the generosity of wealthier farmers. Mr. Mishurov funded renovations to his village's statue of Lenin and a monument to locals who died in World War II, while Mr. Burdin paid to fix up his village's kindergarten.

Mr. Mishurov employs 10 farmhands, three guards and a cook who prepares meals for the workers. "It's a lot for our acreage, but we try to preserve jobs in the village," he said. One recent morning, a man dropped by Mr. Mishurov's farmyard office to cadge a bucket of corn for his hens. It was a former collective farm boss.

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THE WALL STREET JOURNAL.

Business

**Share Buybacks Help Lift Corporate Earnings; Tax cut-fueled repurchases are boosting per-share profits from Apple to Union Pacific and lifting the stock market to new heights**

By Michael Rapoport and Theo Francis
1,058 words
23 September 2018
05:18 PM
The Wall Street Journal Online
WSJO
English


Last December's tax overhaul is boosting corporate profits in more ways than one.

The legislation lowered companies' tax bills, improving their earnings. But the change has also helped them fund record stock buybacks—a move that makes their results appear even better, by boosting the per-share earnings they highlight for investors.

**S&P 500** companies bought back a record $189 billion of their own shares in the first quarter, and a similar number—if not more—is expected for the second quarter, according to S&P Dow Jones Indices. By contrast, **S&P 500** buybacks totaled no more than $137 billion in any of the six quarters before the tax overhaul.

Stock buybacks make profits appear better by boosting per-share earnings, a metric investors frequently use to justify a company's **stock price**. Buybacks reduce a company's share count, spreading the profits across fewer shares. As a result, companies can report a bigger percentage increase in per-share earnings than the profit results alone may show.

Among the more aggressive companies in buying back stock, Apple Inc. repurchased 112.8 million shares in the quarter that ended in June, contributing 5 cents to its earnings of $2.34 a share. Union Pacific Corp. repurchased about 4% of its shares in the second quarter, helping earnings per share climb substantially faster than net income. Thanks to buybacks, Southwest Airlines Co.'s quarterly per-share earnings rose even though its profit fell from a year earlier.

For the **S&P 500**, per-share earnings in the second quarter rose about 25% from a year ago—a full 2 percentage points faster than net income, according to data from Thomson Reuters. "It would be fair to assume it is all from buybacks," said David Aurelio, senior research analyst at Thomson Reuters.

The higher per-share earnings have helped lead investors to pay more for stocks. The **S&P 500 index** is trading at record highs after gaining about 10% this year.

"Investors need to realize what they're paying a premium for," said Howard Silverblatt, senior index analyst at S&P Dow Jones Indices.

In all, dozens of large companies bought back 4% or more of their shares outstanding in the 12 months ended in June, according to data from S&P Dow Jones Indices. The resulting boosts to earnings might seem small in any given quarter, but they add up—Apple's buybacks also added 8 cents a share in the March quarter, for instance. And companies also have started big new buyback programs, suggesting earnings-per-share increases will continue.

The buybacks aren't necessarily done for the express purpose of increasing per-share earnings. Many companies say they want to return excess capital to shareholders. Others intend to offset new shares issued to employees as compensation.

The per-share earnings increases generated by stock buybacks are low quality, inflating results without underlying substance, said Gregory Milano, chief executive of Fortuna Advisors, a financial consulting firm that has examined buyback trends. "It has less value."

Companies play down the buyback effect. They say their earnings are strong even without buybacks, and that while the buybacks add to per-share earnings, the effect is clear to investors and baked into the analyst earnings estimates that drive stock prices.

Apple pointed to its past statements that its earnings growth is accelerating and that tax overhaul "enables us to deploy our global cash more efficiently," leading it to put forward plans to create 20,000 U.S. jobs and invest $350 billion in U.S. operations over the next five years.

Union Pacific's buybacks contributed 9 cents to its second-quarter per-share earnings, helping that metric to climb 37%, while net income rose 29% from a year ago. The railroad's finance chief, Robert Knight, said the buybacks "represent the return of excess cash to our shareholders and are consistent with guidance we provided to the financial-analyst community."

Southwest Airlines' second-quarter net income excluding items declined 2.1% from a year ago. On a per-share basis, however, it rose 2.4%, in part because the company has repurchased 28.3 million shares in the past year. Southwest said its per-share earnings growth "has been driven primarily by the strong financial performance of our robust network."

As the economic cycle grinds on, Mr. Milano said, companies may find it harder to show earnings growth even as they face increased pressure from shareholders to do so--"and so buybacks start to look more attractive."

The buyback effect adds to the earnings boost companies are already seeing because the U.S. cut its corporate tax rate to 21% from 35%. Union Pacific's second-quarter effective rate, for example, declined to 22.1% from 37.5% a year ago, before the tax overhaul. At some companies, the tax cut has accounted for half or more of reported profits.

The benefits to per-share earnings from buybacks can help a company's result compare more favorably to Wall Street forecasts.

In each of the past two quarters, big buybacks by Cisco Systems Inc. increased its adjusted per-share earnings by 2 cents. Each time, the networking giant's total results surpassed analysts' consensus expectations by a penny.

Cisco said its buybacks are incorporated into the earnings per share guidance it provides to analysts. "This is not a quality of earnings issue, and it is inaccurate to state that we would have otherwise 'missed' EPS targets," a company representative said.

Experts say when companies do guide analysts on their buyback plans, the effect on estimates is imprecise. For instance, buybacks earlier in a quarter make a bigger difference in per-share earnings, because such results are calculated using average shares outstanding. Companies, though, don't typically forecast the timing of buybacks.

In the first quarter, just after the tax overhaul, a record 78% of **S&P 500** companies reported earnings above analysts' expectations, according to FactSet. The second quarter then beat that record, with 80%.

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THE WALL STREET JOURNAL.

Markets
**Opportunities to Invest in Private Companies Grow; The number of people allowed to buy into private companies is up 10-fold since the '80s, The Wall Street Journal finds, but such investing can be high-risk**

By Jean Eaglesham and Coulter Jones
1,158 words
23 September 2018
01:00 PM
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English


The Securities and Exchange Commission is drawing up plans to increase the number of people allowed to buy stakes in hot Silicon Valley startups and other private companies. But that population has already grown 10-fold since the 1980s, a Wall Street Journal analysis found.

More than 16 million U.S. households—about one in eight—are already allowed to invest directly in private companies, according to the analysis. Private companies don't have to make the disclosures that public companies do, and regulators thus limit them to only relatively wealthy investors. When the SEC first set its rules of entry for private markets in 1982, only 1.5 million households made the cut.

The reason more households are eligible: The SEC uses income and net worth to determine who can invest, and the thresholds haven't changed in more than three decades.

As private markets boom and the number of public companies shrinks, SEC Chairman Jay Clayton says he now wants to give even more investors the opportunities to buy into fast-growing private companies, such as Uber Technologies Inc. and Airbnb Inc. Further opening access to these markets could ultimately reshape the financial landscape, allowing millions of retail investors to add startups to traded stocks and bonds in their portfolios.

But such investing can be high-risk and more opaque than the public **stock market**—and a draw for fraudsters. Tens of billions of dollars a year of private stakes in companies are now being sold by securities firms with an unusually high number of brokers with three or more investor complaints or other red flags on their records, a recent analysis by the Journal found.

"The biggest area of fraud has always been in these private offerings," said Denise Voigt Crawford, a former Texas securities regulator. "Now you've got more people that are eligible to be the victims of fraud."

An investor typically has to be "accredited" to buy stakes in private companies, which requires an annual income of more than $200,000 or a net worth of more than $1 million—a rule designed to ensure that anyone allowed into these markets can afford to lose what they put in.

The SEC hasn't increased the accredited-investor limits since they were set, apart from a 2012 tweak that excluded primary homes from the calculation of net worth. If the limits had been adjusted to keep pace with inflation, an accredited investor would now need an annual income of about $515,000—more than double the actual $200,000 limit—and a net worth of more than $2.5 million, the Journal found.

Sales of these investments, known as private placements, are expanding rapidly as investors chase profits outside more traditional stocks and bonds. Last year, a record $710 billion was sold through brokers, a nearly threefold rise from 2009, the Journal reported. For this year through August, at least $500 billion has been sold through brokers.

The SEC is expected to seek public comment in coming months on expanding the accredited-investor definition. It is unclear how many more investors would become eligible for the market under the SEC's plan. One addition Mr. Clayton talked about recently is people who don't hit the financial limits but have professional licenses or advanced degrees.

John Harrison, executive director of the Alternative and Direct Investment Securities Association, embraced the SEC idea, saying sophisticated investors "should be allowed that opportunity" and are an essential source of capital for growing the economy.

But Barbara Roper, director of investor protection at the Consumer Federation of America, said the current accredited-investor limits "aren't even remotely adequate to ensure people are protected from potentially devastating losses."

An SEC spokeswoman declined to comment.

Complaints from investors have grown in recent years with the swirl in sales. Arbitration claims relating to two kinds of private markets' investment, private equities and limited partnerships, ballooned from 192 in 2013 to 294 last year, a 53% five-year jump, according to the Financial Industry Regulatory Authority, which oversees the brokerage industry.

Some brokers target people approaching retirement, whose salary or pension savings push them over the accredited-investor thresholds, according to lawyers representing investors. A third of the accredited households are retirees, the Journal's analysis found.

Roy Manson, a former health-care executive in Scottsdale, Ariz., said he wanted a low-risk investment strategy after he retired in 2011. But his Center Valley, Pa., broker, Robert D'Agosta of Berthel Fisher & Co. Financial Services Inc., persuaded him to invest what Mr. Manson said was the "lion's share" of his savings in private placements and other high-risk investments, some of which fell sharply in value. "These sales earned the broker high commissions," said lawyer Christopher Lonn, who is representing Mr. Manson in an arbitration claim due to be heard next month.

"I've had so many sleepless nights," said Mr. Manson.

Mr. D'Agosta and a spokeswoman for Berthel Fisher both declined to comment.

Some regulators and others wonder if financial limits are the best way to decide who has access to private markets.

"Being an accredited investor does not today make you wealthy, and it absolutely does not make you sophisticated," said Douglas Schulz, a former investment adviser who testifies in arbitrations for investors.

Kris Dielman, a former San Diego Chargers guard, and his wife Sandy, for instance, are "entirely unsophisticated financially" and leaned exclusively on their broker, Indiana-based Robert Hoffman, who worked for Woodbury Financial Services Inc., according to an arbitration claim filed by the couple against Mr. Hoffman and Woodbury that was reviewed by the Journal.

In the claim, the broker allegedly told Mr. Dielman that a $450,000 investment in 2007 in a now-defunct company building blimp-like aircraft would increase his net worth by "2m (on paper)." The following year, Mr. Hoffman sold Mr. Dielman a $150,000 stake in a military building in Indiana, writing in an email, according to the claim, "we will ride this thing like a cheap hooker!"

Mr. Hoffman, who Finra barred from the securities industry last year, declined to comment. He agreed to be barred for failing to cooperate with a Finra investigation, without admitting or denying the regulator's findings.

A representative of Advisor Group Inc., which owns Woodbury, didn't respond to requests for comment.

An arbitration panel in June awarded the Dielmans $1.1 million in their claim against Woodbury. Mr. Dielman told the Journal that "this whole thing was bullshit: The guy sleazed me."

Lisa Schwartz contributed to this article.

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THE WALL STREET JOURNAL.

Markets

**OPEC Sees Competition With U.S. Shale Oil Subsiding After 2023; U.S. shale could slow significantly in less than five years, OPEC report predicts**

By Christopher Alessi
607 words
23 September 2018
10:15 AM
The Wall Street Journal Online
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English


ALGIERS—U.S. shale oil production will peak by the late 2020s, triggering renewed demand for OPEC crude after an expected decline and stagnation, the oil cartel said Sunday.

In its latest forecast on the global oil landscape, the Organization of the Petroleum Exporting Countries said it expects U.S. shale growth to "slow significantly" after 2023, before peaking at 14.3 million barrels a day between 2027 and 2028. Output should then fall to an average of 12.1 million barrels a day by 2040, according to OPEC.

The use of hydraulic fracturing in the U.S. to drill for oil in shale rock—known as fracking—has dramatically reshaped the face of the global oil industry over the past decade, rivaling OPEC for market share. Shale was largely behind a glut of American oil that flooded the market over four years ago, leading **oil prices** to fall to $30 a barrel from more than a $100 a barrel in late 2014.

In 2018, U.S. shale production is growing faster than it did during the boom years of 2011 to 2014, the International Energy Agency said earlier this year. The IEA has forecast that U.S. shale oil production will plateau in the late 2020s, while total non-OPEC production should decline.

OPEC projects that "the strongest annual increases are seen in the near-term, in which total U.S. tight oil increases by an average of 1.4 million barrels a day" annually from this year to 2020.

The world's appetite for OPEC crude, meanwhile, should fall to 31.6 million barrels a day in 2023, compared with 32.6 million barrels a day in 2017, before again rising to current levels when U.S. shale supply peaks, the cartel said.

"Thereafter, a gradual decline in non-OPEC liquids supply, coupled with moderate, but sustained global demand growth, leads to a steady increase in demand for OPEC crude, which rises to nearly 40 million barrels a day by 2040," the OPEC report noted.

OPEC's updated outlook comes as the oil cartel is meeting in Algiers with its partner producers, including Russia. The discussion centers on whether producers should raise crude production levels and supply more oil to global markets, amid continued pressure from President Trump to rein in rising prices.

More broadly, OPEC on Sunday also said it expects global demand for oil to increase by an average of 1.2 million barrels a day in the medium-term, reaching 104.5 million barrels a day by 2023. But the cartel said it expects growth to "decelerate over time," reaching 111.7 million barrels a day in 2040. That's up from its forecast last year for 2040 of demand of roughly 107.5 million barrels a day.

The cartel has said it doesn't expect global demand for oil to peak before 2040. That's largely in line with the forecast of the International Energy Agency, which has argued that global oil demand will grow slowly past 2040.

However some international oil majors, including Royal Dutch Shell PLC and Norway's Equinor ASA, predict demand could reach its high as soon as 2025 or 2030. The UK's BP PLC said in February that the world's thirst for oil could grow until around 2035, hitting around 110.3 million barrels a day, before plateauing and falling off in the run-up to 2040.

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THE WALL STREET JOURNAL.

Markets

**Bull Market Charges On, Even Without Tech; The Dow industrials and S&P 500 are at all-time highs, while the S&P tech sector is on course for its worst months since March**

By Akane Otani and James Benedict
524 words
23 September 2018
12:00 PM
The Wall Street Journal Online
WSJO
English


Stocks notched new highs last week. The feat was particularly notable because one of the recent drivers of market gains, the technology sector, has faltered.

Potentially greater regulatory scrutiny of the tech industry put the **S&P 500** technology sector on course for its worst month since March. Yet the resurgence of non-tech sectors, like industrials and health care, has proved the **bull market** has more room to run, investors say.

Shares of industrial companies have rebounded in September as investors bet on a strong economy offsetting uncertainty over global trade policies, helping the **Dow Jones Industrial Average** set a record for the first time since January. But technology-driven companies remain the biggest drivers of the stock rally this year. Amazon.com Inc. and Apple Inc. account for a big chunk of the **S&P 500**'s year-to-date gains, followed closely by Microsoft Corp. and Netflix Inc.

Meanwhile, shares of firms in the consumer staples sector have continued to lag behind the **S&P 500**, hurt by competition from e-commerce giants, changing consumer tastes and rising costs. Cigarette maker Philip Morris International Inc. is one of the five biggest drags on the **S&P 500** this year. The stock has rallied in September, boosted by news that the head of the U.S. Food and Drug Administration is considering banning flavored e-cigarettes.

Going back further, the technology rally looks even more striking. Technology stocks in the **S&P 500** have soared more than 60% since the 2016 election, making them by far the best-performing group in the broad index over that time frame. Consumer-discretionary stocks, boosted by heavy-hitters like Amazon.com Inc. and Netflix Inc., have fared well, too.

Some investors have cited the dominance of the two sectors as reason to worry that the nine-year **bull market** is on shaky ground: fund managers surveyed by Bank of America Merrill Lynch have identified the FAANG group, as well as its Chinese counterparts, as the most crowded trade in the markets for eight consecutive months. But the fact that the **stock market** has charged higher even with technology stocks retreating in September has reassured many investors that the rally still has room to run.

The resurgence of stocks outside of the technology sector has helped the **Dow Jones Industrial Average** hit new highs again after an eight-month record drought.

Even after hitting a string of new records, the **stock market** looks less pricey than it did in January.

But another measure of stock valuations, which compares stock prices to their inflation-adjusted earnings from the past decade, suggests stocks are the most expensive they have been in years. Some investors are warning that stretched valuations could leave the market vulnerable to a pullback, should the tech trade stumble or economic data start disappointing.

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THE WALL STREET JOURNAL.

Markets

**Smoke Gets in Your Eyes, Investor Edition; Turnover of popular pot stocks is far in excess of that for far larger, more-established companies on U.S. exchanges**

By Spencer Jakab
193 words
23 September 2018
09:03 AM
The Wall Street Journal Online
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English


It is easy to see why investors got interested in marijuana. While a handful of U.S. states have or are in the process of legalizing its recreational use and still more for medical use only, its federal prohibition leaves it in legal limbo. But now Canada, a whole country, will allow recreational sales next month—a brand new legitimate industry.

The rush of large corporations such as Coca-Cola and Constellation Brands to the bandwagon has further stoked excitement. Consider, though, that just one listed pot company, Tilray Inc., had share turnover on **Nasdaq** of over $30 billion so far in September as of Friday morning as its price gyrated wildly. That is more than blue chips IBM, General Electric and Exxon Mobil combined. It is also about six times the projected amount of Canadian marijuana sales in four years.

People just need to chill out and see what happens.

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The New York Times

STRATEGIES
Money and Business/Financial Desk; SECTBU
**Why Trade Disputes Are More Than a Money Problem**

By JEFF SOMMER
1,328 words
23 September 2018
The New York Times
NYTF
Late Edition - Final
3
English


The Trump administration's ''America First'' approach to tariffs and trade doesn't merely involve financial issues: It raises questions central to war and peace.

That may sound hyperbolic. But two Yale law professors, Oona A. Hathaway and Scott J. Shapiro, make a persuasive case that the world could become a far more dangerous place if the Trump administration seriously disrupts the global consensus that has been in place for decades.

''Imperfect as it may be, the world operates under the understanding that war is illegal and trade sanctions are a legal method of punishing aggressive behavior,'' Professor Shapiro said. ''But sanctions only work with a healthy regime of international trade, and under the rule of international law. That is all coming into question now.''

For the moment, the most obvious issues arising from the Trump administration's trade initiatives are mainly financial. On Monday, the United States imposed new tariffs on $200 billion in Chinese goods, and Mr. Trump said he was prepared to tax all Chinese imports.

The Chinese authorities quickly retaliated with new levies on $60 billion in American products. And the United States also has trade disputes brewing with several allies. The costs for consumers, businesses and the world economy are being closely tallied.

[Keith Bradsher, our Shanghai bureau chief, answers questions on the trade war and the global economy on Facebook Live.]

But the two scholars say the administration's aggressive approach could have a much higher cost: It could unravel a complex series of rules and agreements that have served to moderate the behavior of great powers like the United States, China, the Soviet Union and, now, Russia.

In a provocative book, ''The Internationalists: How a Radical Plan to Outlaw War Remade the World'' (Simon & Schuster, 2017), they provide a history of international law. They say the relative prosperity and peace of the post-World War II world owes a great deal to a now-obscure international treaty -- the Kellogg-Briand Pact.

The treaty, signed in 1928, outlawed war. That may seem an odd statement, because, of course, war never ended. World War II was the most costly conflict in human history, terrorism and intrastate violence have flourished around the world, and the Afghanistan conflict is already the longest-running American war by a large margin.

Perhaps that is why the Kellogg-Briand Pact is often belittled, when it is remembered at all. George Kennan, the eminent diplomat, historian and strategist, called the pact ''childish, just childish'' in its utopian aspirations.

Yet the book makes a spirited argument that a series of legal and institutional changes gradually flowed from that 1928 treaty, helping to create the rules of a world order that are now as pervasive -- and as little noticed -- as the air we breathe. And in interviews, the two professors said the Trump administration's actions and threats are endangering that stabilizing environment.

It's not just that allies like China, Germany, Japan and Canada say they are preparing reciprocal measures in response to the rising tariffs threatened or imposed by the United States. It's not just that **financial markets** and economic sectors have begun to react, or even that the escalating trade war threatens global economic growth. It's not even the increasingly acrimonious relationship between China and the United States.

At stake are even bigger issues, the professors say.

Consider, Professor Hathaway said, what kind of a world we could be re-entering, if the Trump administration's escalation of its conflicts with other nations were to shred the current international consensus.

"Some pivotal principles are at stake," she said. "Recall that punishing aggressive behavior through trade sanctions was illegal before the treaty in 1928, and acquiring territory through war was legal," she said. "But in 1928, and with the rules that gradually developed, that was reversed."

She continued: "It's important to realize that if you disrupt the world trading system -- and the consensus outlawing war that is in place today -- you are disrupting the financial means of punishing violations of war. In the end, you may be left with nothing but reliance on force."

Without robust trade, she said, geopolitical disputes over such issues as dominion over the South China Sea could flare more easily into military confrontations between great powers. Mutually beneficial commerce -- and the need to abide by the international rules that make it possible -- have successfully moderated the behavior of sovereign states.

That has been the explicit aim of a succession of United States presidents, starting with Richard M. Nixon, who sought to give China -- formerly an isolated Communist giant -- a stake in the world economy and in the American-dominated global economic and political system put in place in the aftermath of World War II.

This has never been entirely smooth. Disagreements over the terms of trade and the structure of the Chinese economy have rankled Americans since the early 1980s, when China entered the modern world economy. But given their political and economic differences, China and the United States have had a remarkably calm relationship until now.

Strong, respectful negotiating to improve the relative standing of the United States is entirely appropriate, Professor Shapiro said. "I don't think anybody would defend the current system as being perfect. Far from it. But there's a difference between trying to reform the system from within, and blowing it up, which is what seems to be happening."

For example, he said, the day-to-day rules and arbitration procedures of the World Trade Organization don't usually attract much attention, but they are crucial if trade is to proceed smoothly -- and peacefully -- around the world.

By invoking national security provisions to support its trade demands, the president has helped to create a crisis at the organization. And by blocking the appointment of the appellate judges who arbitrate disputes, the administration is making it difficult for the W.T.O. to address the increasingly contentious trade fracases that have been erupting ever more frequently.

The situation has become bad enough that the European Union has started a "last-ditch effort" to repair the W.T.O. and save it from what may well be the Trump administration's efforts to destroy it, Politico reports.

And the administration's decision to abandon the Trans-Pacific Partnership trade deal and to use high-pressure tactics to rework or abandon the North American Free Trade Agreement epitomize the "go it alone approach" that President Trump has used, breaking with the traditions of every other post-World War II presidency, Professor Shapiro said.

As a prime example of the administration's animus toward international organizations, Professor Hathaway pointed to a Sept. 10 speech by John Bolton, President Trump's national security adviser, in which he attacked the International Criminal Court in The Hague. Mr. Bolton said the organization -- established through a treaty signed by 123 states -- "unacceptably threatens American sovereignty and U.S. national security interests."

In a remarkable turnabout, he threatened to use economic sanctions -- which became a prime tool for enforcing international law as a result of the Kellogg-Briand Pact -- as weapons to deter the court's judges from enforcing international law, Professor Hathaway said.

Furthermore, Mr. Bolton has in the past condemned the W.T.O. as well, generally advocating a unilateral approach by the United States and an end to the decision-making process enshrined in the organization.

Under the circumstances, boring, negotiated resolutions to the current trade disputes would be a happy ending, Professor Hathaway said. What the world may face instead, is the dismal prospect of conflict without the rules or means for resolving it peacefully. The United States would remain a powerful player in that world, but it would be playing a much more dangerous game.

Follow Jeff Sommer on Twitter: @jeffsommer

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THE WALL STREET JOURNAL.
U.S. EDITION

**EXCHANGE --- Heard on the Street: Triumph of The Pessimists --- A 'Black Swan' fund that has managed to make money in a great bull market**

By Spencer Jakab
783 words
22 September 2018
The Wall Street Journal
J
B14
English


[Financial Analysis and Commentary]

The 10th anniversary of the financial crisis is a natural time to fret about the next bust, but betting against the market is usually a loser's game. Or is it?

Record stock prices, bubbling trade wars, Donald Trump's legal peril and sputtering emerging markets give some teeth to fears of another market rout. So did a host of mostly forgotten crises -- Brexit, the fiscal cliff, the taper tantrum -- that turned out to be great buying opportunities. The **S&P 500** has returned over 200% since the day Lehman Brothers went bust -- more fodder for the investing classic "Triumph of the Optimists" that underlines the benefits of staying in the market through thick and thin.

So why is a man who has made a huge wager on another market collapse so happy? It isn't because he sees an imminent crash, though he doesn't rule it out. It is because almost no one else is preparing for one.

"I spend all my time thinking about looming disaster," says Mark Spitznagel, chief investment officer of hedge fund Universa Investments, who predicts a major decline in asset prices but can't say when. He admits that the **bull market** could keep going for years. "Valuations are high and can get higher."

Talk is cheap in investing punditry and predicting a decline without saying when it will happen is cheapest of all. Yet Universa's stance warrants attention, and not only because it backs its views with billions of dollars and is advised by author Nassim Nicholas Taleb of "Black Swan" fame. Mr. Spitznagel isn't betting on some unpredictable event causing a crisis but a predictable one -- an eventual blowback from unprecedented central-bank stimulus.

What sets the fund apart and why investors should pay attention is that Mr. Spitznagel's clients have done well without a crisis. Founded in 2007, Universa was among a handful of funds that made huge gains in 2008. Unlike some crisis-era legends such as John Paulson, David Einhorn and Steve Eisman who have struggled mightily since then, Mr. Spitznagel has enjoyed minibonanzas along the way. In August 2015, for example, his fund reportedly made a gain of about $1 billion, or 20%, in a single, turbulent day.

A letter sent to investors earlier this year said a strategy consisting of just a 3.3% position in Universa with the rest invested passively in the **S&P 500** had a compound annual return of 12.3% in the 10 years through February, far better than the **S&P 500** itself. It also was superior to portfolios three-quarters invested in stocks with a one-quarter weighting in more-traditional hedges such as Treasurys, gold or a basket of hedge funds.

Being skeptical and making money on that view are two different things. Fellow financial crisis standout John Hussman predicted both the 2000 and 2008 bear markets and also is convinced an even worse one is coming, yet his eponymous fund has performed dismally since 2009, eroding its crisis gains and then some.

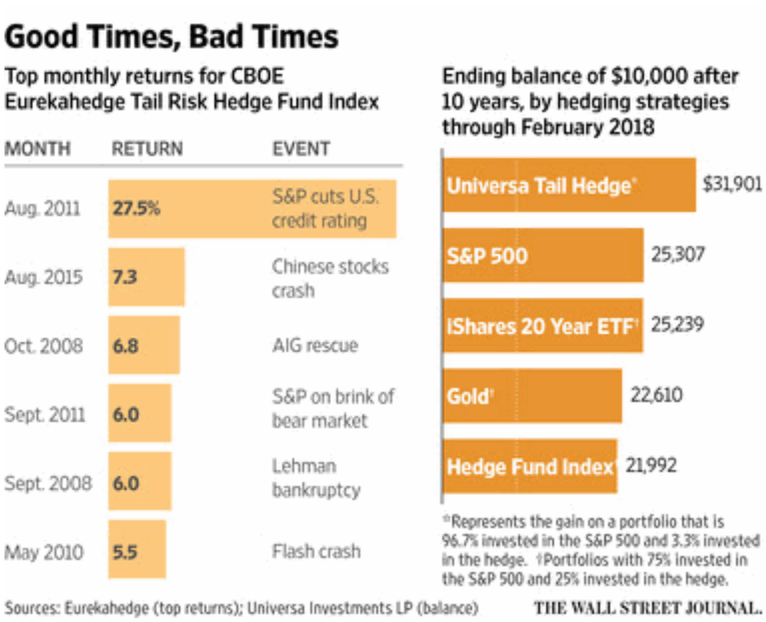
While Mr. Hussman tries to identify dangerous junctures and hedges his fund accordingly, Mr. Spitznagel has no view on timing. Instead, he buys hedges, typically put options, particularly when they are cheap. These options rise in value when the market falls but usually expire worthless. The approach is a variation on the well-proven strategy of value investing -- buy cheap, unloved assets. By pointedly ignoring headlines and embracing long stretches when his fund loses small sums for months on end, he draws on similar patience and conviction.

In a banner year for U.S. stocks like 2017, buying crash insurance was like throwing money away. But Mr. Spitznagel says he was "like a kid in a candy store" because **volatility** -- and hence options prices -- was so subdued.

Just sitting out the market in the long run is costly, which is why optimists triumph. Universa's typical client suspects that the end may be nigh but wants to stay fully invested anyway. The occasional windfall, such as the one in 2015, is icing on the cake.

Ordinary investors don't need to understand Mr. Spitznagel's math to grasp a valuable lesson. While human nature causes us to be more confident after a long stretch of smooth sailing and hefty gains for markets, that is when the chances of something going horribly wrong are highest.

"This is a very good time for us," he says.

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THE WALL STREET JOURNAL.
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**EXCHANGE --- The Score: The Business Week in 6 Stocks**

By Laine Higgins
715 words
22 September 2018
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English


**DOW JONES INDUSTRIAL AVERAGE**

DJI +0.95%

The 30-stock **Dow Jones Industrial Average** passed its Jan. 26 high to close at a record of 26656.98 on Thursday, a sign that upbeat economic conditions are outweighing investors' concerns about trade tensions. The **S&P 500** also notched a record close Thursday of 2930.75, besting the mark set Aug. 29, and the **Nasdaq Composite** Index finished within 1% of its high. The Dow extended its record Friday, but the other indexes fell.

SANDERSON FARMS INC.

SAFM -1.5%

Flooding from Hurricane Florence left a trail of devastation across North Carolina's poultry and hog industries. State officials said Tuesday that 5,000 of the state's 8.9 million pigs and hogs were killed, as well as 3.4 million chickens and turkeys. Sanderson Farms said it lost 1.7 million of its roughly 20 million broiler chickens, though it said it experienced no significant damage to its processing facilities, feed mill or hatcheries in the state and expected insurance to cover a substantial portion of damages. Shares of Sanderson, the country's third-largest poultry producer, fell 1.5% on Monday.

AMAZON.COM INC.

AMZN -3.2%

As Amazon works to stop seller scams and fake reviews, it's turning its focus to its own employees. The Wall Street Journal reported Sunday that the e-commerce giant is investigating suspected data leaks and bribes in which employees, often with the help of intermediaries, offered internal data and other confidential information that can give an edge to independent merchants selling their products on the site. The suspected violations of company policy have been most pronounced in China, though some U.S. employees have also been investigated. Shares declined 3.2% Monday.

TILRAY INC.

TLRY +38%

Shares of Canadian marijuana producer Tilray Inc. were lit up this past week, climbing 38% on Wednesday after gaining as much as 96% intraday on news that the U.S. Drug Enforcement Administration granted permission to import the drug for a clinical research trial at the University of California, San Diego. The company's stock has soared more than 800% since its July initial public offering and is one of many cannabis-related stocks that have been on fire in the months ahead of Canada's October legalization of recreational marijuana use.

GENERAL MILLS INC.

GIS -7.6%

General Mills' effort to offset sluggish sales of human food with sales of animal food hit a snag last quarter. While sales at the company's pet-food division, which includes the newly acquired Blue Buffalo, rose 14% from the year-earlier quarter, that represents a slowdown from Blue Buffalo's stand-alone growth. Overall sales rose 8.6%, but sales in the company's main North American market fell 2.1%, more than analysts expected. Chief Executive Jeff Harmening expressed confidence in the pet-food business, but General Mills shares, down about 25% this year, fell 7.6% Tuesday.

UNDER ARMOUR INC.

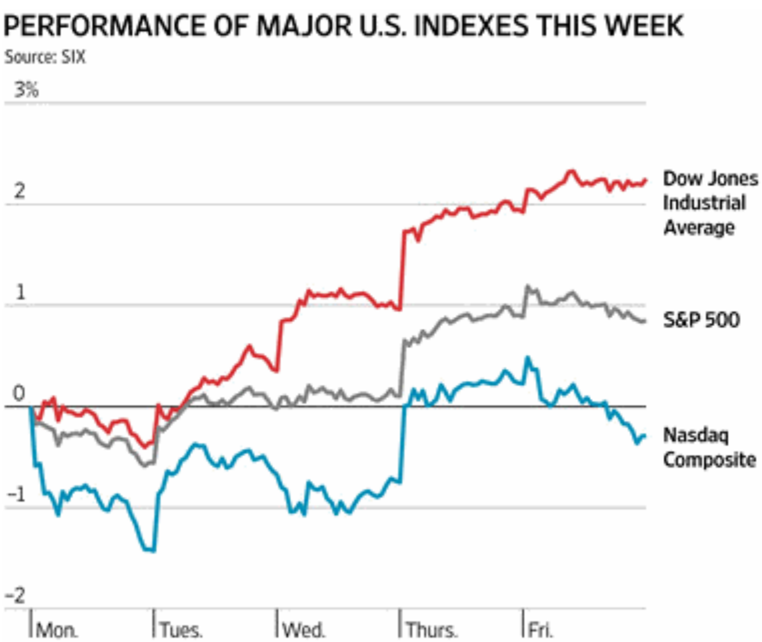
UAA +6.6%

Under Armour said Thursday that it plans to reduce its global workforce by about 400 employees, the athletic retailer's latest attempt to cut costs and combat weak sales figures. The layoffs will add $10 million in pretax restructuring charges and come a little over a year after Under Armour eliminated 280 jobs as part of what CEO Kevin Plank at the time called a "reset." Under Armour expects the move to help its bottom line and raised the low end of its adjusted earnings guidance for 2018, giving Class A shares a 6.6% boost on Thursday.

TWITTER INC.

TWTR -4.5%

The **S&P 500** got a major shakeup Friday, as the index reclassified 23 companies -- including Twitter, Facebook Inc. and Google parent Alphabet Inc. -- valued at a combined $2.7 trillion. With the reshuffling, the **S&P 500**'s former telecom sector is now called "communications services" and includes high-growth former tech companies, an attempt to rebalance the segment after industry consolidation shrunk membership to just three stocks. Shares of Twitter were down 4.5% on Friday, while Facebook and Alphabet lost 1.9% and 1.6%, respectively.

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**A Mixed End for Markets**

By THE ASSOCIATED PRESS
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Wall Street capped a milestone-setting week on Friday with a mixed finish for the major stock indexes and the second record high in two days for the **Dow Jonesindustrial average**.

An afternoon sell-off erased modest gains for the **Standard & Poor's 500-stockindex**.

Losses for technology companies and retailers offset gains in energy and industrial stocks.

''When you have a big up week like we've had, we're at all-time highs, for people to take a little bit of risk off the table going into the weekend isn't a big surprise,'' said Randy Frederick, vice president of trading and derivatives at Charles Schwab.

The **S.&P. 500** dropped 1.08 points, or 0.04 percent, to 2,929.67, just under its latest record high set a day earlier. The Dow gained 86.52 points, or 0.3 percent, to 26,743.50, thanks largely to gains in Boeing and McDonald's.

The **Nasdaq composite** lost 41.28 points, or 0.5 percent, to 7,986.96. The Russell 2000 index of smaller companies gave up 7.87 points, or 0.5 percent, to 1,712.32.

The Dow and **S.&P. 500** each ended the week with their 10th weekly gain in the past 12 weeks.

Shares of the chip maker Micron Technology were among the biggest decliners in the technology sector. Micron said its profits would be hurt by new tariffs on Chinese imports that go into effect next week. Shares in the company slid 2.9 percent to $44.74.

The trade dispute between the United States and China is set to escalate Monday, when an additional 10 percent tax on $200 billion of Chinese imports kicks in. The tariffs will rise to 25 percent on Jan 1. Beijing has said it would retaliate by imposing tariffs of 5 or 10 percent on $60 billion of American goods, including coffee, honey and industrial chemicals.

Other sectors fared better Friday. Shares of several airlines rose, part of a broad pickup in industrial sector stocks. American Airlines Group stock climbed 4.1 percent to $43.60 after the company said it would raise fees for checked bags. The move came a day after Delta Air Lines announced its own plans to raise baggage fees. Delta shares added 2.5 percent to $59.61. Southwest Airlines stock rose to $63.77.

Mazor Robotics stock surged 10.2 percent to $58.15 after the company, which makes surgical guidance systems, agreed to be bought by Medtronic for $1.54 billion.

Benchmark United States crude gained 0.7 percent to settle at $70.78 a barrel in New York. Brent crude, used to price international oils, added 0.1 percent to close at $78.80 a barrel in London.

**Bond prices** were little changed. The yield on the **10-year Treasury** held steady at 3.07 percent.

The dollar rose to 112.55 yen from Thursday's 112.40 yen. The euro edged down to $1.1747 from $1.1776. The British pound weakened to $1.3079 from $1.3269 after Prime Minister Theresa May of Britain said talks over leaving the European Union were at an impasse.

Gold fell 0.8 percent to $1,201.30 an ounce.

CHART: The **S**.**&P**. **500 Index**: Position of the **S**.**&P**. **500 index** at 1-minute intervals on Friday. (Source: Reuters)

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**EXCHANGE --- Saudis Strain to Head Off Oil-Price Rise**

By Summer Said and Benoit Faucon
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B12
English


ALGIERS, Algeria -- Saudi Arabia is running low on its most prized grade of crude, people familiar with the matter said, a development that could push **oil prices** higher.

After coming under pressure from the Trump administration over rising **oil prices**, Saudi Arabia is set to use an oil-producers' summit in Algiers on Sunday to reassure oil markets that it can fill any shortages that arise as U.S. sanctions restricting Iranian oil sales begin in November.

But state-run oil giant Saudi Arabian Oil Co., known as Aramco, is telling potential buyers that its most highly prized crude will be in short supply in October after it underestimated the demand in advance of Iranian sanctions. And in the longer term, officials estimate Aramco wouldn't have the capacity to meet future demand if Iran is no longer delivering oil, according to people familiar with the matter.

The scarcity could push prices above $80 a barrel, potentially putting a strain on U.S. consumers as they decide whether President Trump's Republican Party will remain in control of both houses of Congress in November's midterm elections.

With the combination of Iran sanctions and Saudi Arabia's supply limitations, "we are heading to a price spike, likely $90 to $100" per barrel, one oil trader said. "It's not just Iran that will suffer. It's going to have a boomerang effect with rising gasoline prices" in the U.S., the trader said.

Aramco's Arab light crude has been in high demand from buyers ahead of Iran sanctions, one potential buyer said he was told this week, and as a result, supplies have been fully allocated for October. The buyer says he was offered Aramco's less popular medium and heavy oil.

Saudi Arabia says it increased overall oil production by 400,000 barrels a day in the past two months after coming under pressure from the U.S. The country now produces roughly 10.4 million barrels a day. A day after **oil prices** reached $80 a barrel, Mr. Trump said Middle East producers "continue to push for higher and higher **oil prices**" in an early morning tweet Thursday.

Mr. Trump has previously said Saudi Arabia's King Salman told him the kingdom could bring its production to 12 million barrels a day.

Such a level would mean the Kingdom -- the only producer able to significantly adjust its production at will -- could cover much of Iran's current exports of 1.9 million barrels a day if the U.S. achieves its goal of banning the sale of all Iranian oil.

Internally, some Saudi officials estimate it couldn't sustain such a level, according to people familiar with the matter. Producing "11 million is already a stretch, even for just a few months," one Saudi official said. Spokespeople for the Saudi energy ministry and Aramco didn't return requests for comment.

Another person briefed on Saudi production capacity said the Kingdom could pump at 11 million for only six months. A senior U.S. official said Washington estimates Saudi Arabia couldn't reach 12 million barrels a day.

Saudi officials said they are comfortable with current price levels, but they worry a further rise could decrease demand and bring a subsequent price collapse.

Some relief to the Saudi supply problem could come from oilfields shut down for three years over a dispute between the Kingdom and Kuwait. Until recently, both sides had little incentive to resume production in an oversupplied market.

But the two countries are now finalizing a resolution of differences over environmental and land permits, according to people familiar with the matter.

As a result, Saudi Arabia and Kuwait are getting ready for the possible resumption of the 300,000-barrels-a-day facility at the Khafji field by early next year, and possibly as early as December, they said.

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Sarah McFarlane contributed to this article.



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**EXCHANGE --- The Intelligent Investor: No Need to Be Spooked By the Turn of the Season**

By Jason Zweig
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English


Every year, as the end of summer approaches, monarch butterflies head for Mexico, birds migrate south for the winter, and financial pundits predict that the **stock market** is about to crash. Is the longstanding popular belief that September and October are the worst months for stocks valid?

Yes and no -- mostly no.

Yes, some of the worst days in Wall Street's history have hit during September and October.

On Sept. 24, 1869, the original Black Friday, the price of gold collapsed roughly 20% and took the **stock market** down with it.

On Sept. 18, 1873, the investment bank Jay Cooke & Co. suspended payments, setting off a series of bank failures that triggered one of the worst depressions in U.S. history.

On Oct. 16, 1907, a busted speculation in copper led to a run on some of New York's biggest banks, sparking a panic that ended only when J.P. Morgan personally intervened -- ultimately leading to the creation of the Federal Reserve.

On Oct. 28, 1929, "Black Monday," the **Dow Jones Industrial Average** lost 12.8% in the crash that set the stage for the Great Depression.

On Oct. 19, 1987, the Dow fell 22.6%, the worst daily loss in its history.

On Sept. 15, 2008, Lehman Brothers failed, ushering in the darkest days of the global financial crisis.

Is this destiny, or just random variation?

According to William Schwert, a finance professor at the University of Rochester who studies the history of asset prices, September does have the lowest average return of any month. From 1834 (the earliest date for broad market data) through 2018, September is the only month whose average return is negative -- at minus 0.4%.

But the differences across months have been small, so you shouldn't read much into September's relatively poor historical average return, cautions Prof. Schwert.

Over the long run, December has the best average monthly return, at nearly 1.4%, with January close behind at 1.2%. The variations "don't have much economic significance," says Prof. Schwert.

As for October, its returns are positive on average, at 0.4% since 1834. Since 2002, October is the third-best month, with an average 1.6% return -- even though the **S&P 500** lost nearly a fifth of its value in October 2008.

So investors' fear of September and October is based less on evidence and more on what psychologists call "availability" -- the human tendency to judge how likely an event is by how easily we can recall vivid examples of it. The horrific losses of October 2008 are hard to forget. The milder gains of 7% in October 2015 and 11% in October 2011 are hard to remember.

Investors might be more prone to worry this time of year, though. Researchers have found in numerous independent studies that as summer fades into fall, people's behavior does turn with the leaves. As the hours of daylight dwindle, brain chemistry can change, reshaping how much risk some people are willing to take.

In his 1903 book, "The ABC of Stock Speculation," the financial chronicler Samuel Armstrong Nelson wrote: "Speculators are not disposed to trade as freely and confidently in wet and stormy weather as they are during the dry days when the sun is shining, and mankind cheerful and optimistic."

Investors trading options are more likely to expect losses in fall than in spring or winter. In the U.S., Canada and Australia, mutual-fund shareholders are all net sellers in their respective fall months, even though Australia's autumn runs from March through May and it has a different tax year.

Average returns on U.S. Treasurys appear to be higher in fall than in spring, suggesting that investors seek safety in the darker months. Stock analysts' earnings forecasts are less optimistic in fall and winter than in spring and summer.

Of course, not all investing decisions are driven by psychology. Nowadays, people might tend to sell stocks in the fall in order to fund tuition payments coming due in September or to pay off credit-card debt they racked up on summer vacations. They might invest more in the first quarter of the year after pocketing year-end bonuses and tax refunds.

Still, "if bad news comes out in the fall, many investors may react more extremely than they might a few months later or earlier, when daylight is more plentiful," says Lisa Kramer, a finance professor at the University of Toronto who has run several studies on how seasonal mood changes may affect financial behavior.

Although the **stock market** doesn't always crash in the fall, you might well be more likely this time of year to treat smaller declines as harbingers of doom. Try, instead, to remember that the darkest months of the year often have the brightest returns.



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**EXCHANGE --- U.S. Crude Prices Climb Ahead of OPEC Meeting**

By Sarah McFarlane and Dan Molinski
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B12
English


Oil prices climbed back toward two-month highs Friday as investors wagered that this weekend's meeting of major oil producers in Algeria won't do much to reverse a trend toward tighter global supplies.

Light, sweet crude for November delivery settled 0.7% higher at $70.78 a barrel on the New York Mercantile Exchange. Brent crude, the global benchmark, rose 0.1% to $78.80 a barrel.

The U.S. benchmark oil price has risen four of the past five weeks and is 8% higher than it was one month ago.

A monitoring committee meeting on Sunday between the Organization of the Petroleum Exporting Countries and nonmembers, including Russia, is expected to feature discussions around offsetting lower Iranian exports with production elsewhere. Added production could have the effect of lowering oil prices, though much would depend on the size of any output increase.

Oil prices were higher across the board early Friday morning but fell briefly midmorning after a report from Reuters, citing unnamed sources, indicated OPEC and nonmembers would be discussing raising output by 500,000 barrels a day. But analysts said skepticism remains that any major output boost will be agreed upon at the meeting, and oil prices soon rebounded.

President Trump inserted Washington's position into the discussion on Thursday, posting a tweet that said OPEC should stop pushing for higher oil prices, and demanding that "the OPEC monopoly must get prices down now!"

U.S. oil prices have risen by $20 a barrel over the past 12 months, helping send the average gasoline price for drivers in the U.S. toward a multiyear high of $2.88 a gallon Friday. That is 30 cents a gallon more than this time last year, according to price-tracking firm GasBuddy.

Stewart Glickman, head of energy research at CFRA Research, said such tweet storms by Mr. Trump in advance of the U.S. midterm elections in November could pressure the Saudis to expand production. But he said that doesn't mean that the Saudis can or will do so.

"We are not optimistic that Saudi Arabia will agree to sharply boost production, even as it owns the lion's share of global spare capacity, around 60%, per the IEA," he said. "The problem? Opening up the spigots might not be sustainable and imperil long-term production capabilities."



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