THE WALL STREET JOURNAL.
U.S. EDITION

Heard on the Street
Trade Fight Set to Squeeze Investors

By Justin Lahart
470 words
25 June 2018
The Wall Street Journal
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B9
English

[Financial Analysis and Commentary]

With their escalating trade feud showing little evidence of hurting their economies, the U.S. and China aren't close to backing down. Investors may get squeezed between the two giants before one of them cracks.

The U.S. already has put tariffs on steel and aluminum and will add a 25% tariff on $50 billion in Chinese imports starting next month. China is matching the U.S. tariff for tariff. These actions have sent U.S. steel prices higher and U.S. soybean prices lower. But the broader economic effects so far appear negligible.

That could change soon. The administration is set to announce restrictions on Chinese investments in the U.S. next week, and President Donald Trump has threaten-ed to retaliate against China's retaliation and put tariffs on more goods.

The administration thinks that China has more to lose in this dispute, since China runs a big trade surplus with the U.S. The real issue isn't who has more to lose but how long each side can bear the pain. This is where it could get dangerous for investors. Worries about what could come next weighed heavily on shares of companies that depend on China for business, such as Caterpillar and Boeing, last week.

The next round of tariffs against China, if it comes, will likely hit consumer goods. As a result, it won't affect just Chinese producers, but also U.S. retailers (if they absorb the cost increases) or U.S. consumers (if the price increases get passed on). This is particularly true for the many goods dominated by Chinese production, such as cellphones and footwear, where the ability to find other sources is limited. A lot of those China-made goods are produced by U.S. multinationals, so they, and their investors, will share in the pain.

China could also make things difficult for U.S. multinationals by stepping up regulations against them or encouraging Chinese consumers to avoid their products. And it has ways to blunt the impact of U.S. trade actions, such as supporting affected Chinese exporters and lowering the value of its currency.

China's leaders may not back down until there are serious economic or social consequences from the trade fight. The government has the ability to control the Chinese **stock market**, and leaders don't have to worry about elections. The White House does have to pay attention to the **stock market**, since sharp declines inevitably stoke economic fears. And it has midterm elections coming up.

Until one of those tripwires gets hit, the trade fight could get more pitched, leaving investors to absorb the blows. It could be an interesting summer.

Weak Harvest

Soybean near-month futures

$11.00 a bushel

Source: FactSet

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THE WALL STREET JOURNAL.
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World News: China Eases Credit as U.S. Tariffs Loom --- Cut in bank reserve requirement aims to support growth as trade war heats up

By Lingling Wei and Chao Deng
1,008 words
25 June 2018
The Wall Street Journal
J
A5
English

BEIJING -- China's central bank is freeing up more than $100 billion for commercial banks to boost lending and restructure debt, as the Chinese leadership tries to shore up growth amid slowing momentum for economic expansion and an intensifying trade brawl with the U.S.

In a statement Sunday, the People's Bank of China announced it is reducing the amount of reserves banks are required to keep with the central bank by half a percentage point starting July 5. That is the day before a U.S. deadline to slap punitive tariffs on tens of billions of dollars in Chinese goods.

Under the reserve cut, some 500 billion yuan ($76.86 billion) will be released for 17 large banks, including the Big Five state-owned banks, the central bank said. It said the banks are to use the freed-up funds by converting bad loans into equity in companies that default on their debts.

Another 200 billion yuan is being unleashed for the country's city-level commercial banks and other smaller lenders, and those funds are to be used to expand lending to small businesses, the central bank said in the statement.

The move was well-flagged, following a notice last week from the governing State Council urging more measures to help small firms. Still, it marks a shift in policy toward easier access to funds for lenders and away from the tightfisted credit controls imposed in recent years to keep in check already high debt levels that could choke growth long term.

That change, government advisers and economists said, reflects Chinese leaders' desire to shore up growth, stabilize **financial markets** and alleviate concerns that the trade fight with Washington will batter an economy that is losing steam.

After shares on Chinese exchanges followed global markets downward Tuesday on fears of an outright trade conflict, Liu He, President Xi Jinping's economic captain, dispatched central-bank Governor Yi Gang to talk to state media to try to calm jittery investors, according to people with knowledge of the matter. In an interview, Mr. Yi pledged to use monetary policy "comprehensively" to fend off any "external shocks."

Following the reduction in banks' reserve-requirement ratio, analysts expect more loosening, including increasing lending quotas for banks, relaxing mortgage restrictions for home buyers in some cities and easing limits on local governments to borrow.

"China is on the way toward monetary easing," said Zhu Chaoping, a Shanghai-based global market strategist at J.P. Morgan Asset Management.

The shift is tricky, potentially aggravating voluminous levels of corporate and government debt and reflating asset bubbles Beijing has fought hard to control. In some previous reserve reductions, banks have had to meet central-bank criteria for lending to small businesses to lower their reserves. For the latest move, the central bank didn't impose such a condition.

The reduction also tries to jump-start a two-year-old loan-relief plan that is supposed to help big corporate borrowers cut their debt but that the banks dislike. Under the debt-for-equity plan, companies give equity to their lenders in return for debt forgiveness. But in accepting equities of questionable value, banks were required to bump up capital they set aside against these riskier holdings, constraining their liquidity.

By releasing more long-term funds for the big banks, the central bank said it wants to encourage these lenders to step up their debt-for-equity restructurings. The central bank also warned the big lenders against using the funds to make more loans to struggling corporate borrowers.

Targeted easing measures hasn't worked well in the recent past. In 2015, for instance, reserve requirements were cut for select banks four times to channel more financing for small businesses. Funds continued to flow to state-owned firms, causing their debt loads to keep climbing well into 2016, while private companies pared their leverage during that time, according to research firm Gavekal Dragonomics.

Meanwhile, the selective loosening also contributed to frenzied home buying in many big cities, prompting the government to reinstate tight mortgage and other restrictions to curb speculation. "The tendency will be for the liquidity to leak to other parts of the system, most likely property, where the moral hazard problem remains as great as ever," said Gene Frieda, London-based global strategist at Pacific Investment Management Co.

Bank Move Comes

As Growth Shows

Signs of Waning

Property investment, more government spending on infrastructure and a surprising boost from exports to a rebounding U.S. and Europe kept the Chinese economy humming most of the past two years. That allowed President Xi Xinping to focus on curbing the growth of debt and other financial risks that economists have cited as a long-term vulnerability for the world's second largest economy.

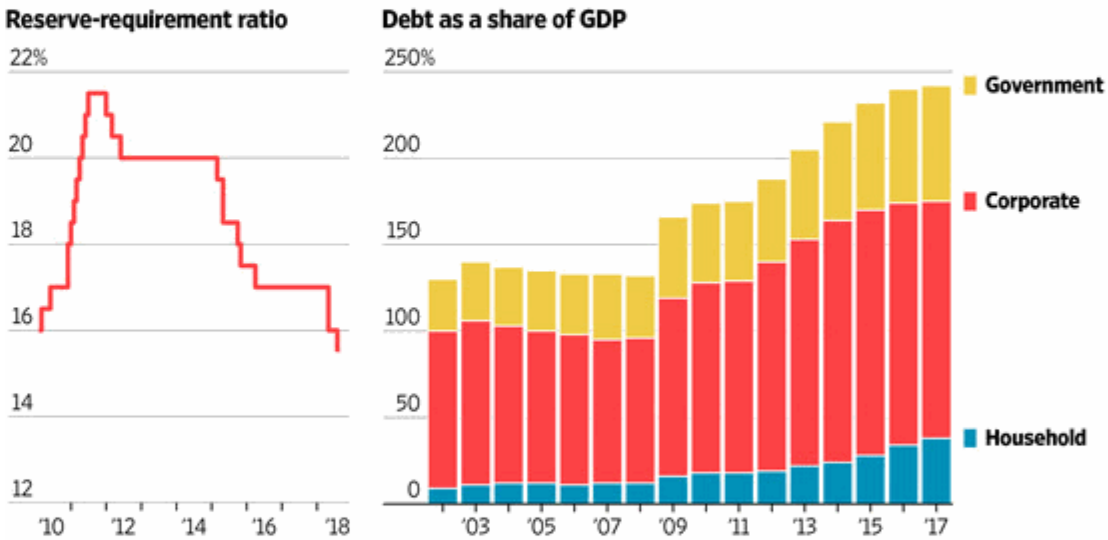
Chinese growth is showing signs of waning -- from investment in fixed assets to household consumption -- and corporate defaults are rising, especially by private companies squeezed by the debt controls.

So far, the trade fight, initiated by the U.S. to reduce a trade imbalance $375 billion in Beijing's favor last year and to get China to end policies Washington says favor Chinese companies, has been mostly words. In April, the central bank cut the reserve requirement pre-emptively to allay worries that the trade battle would hit the economy.

Should the U.S. impose tariffs on $34 billion of Chinese goods early next month as the White House has planned, that would shave 0.1 percentage point off China's growth in the first year, according to economists. The damage could rise to 0.3 percentage point if the tariffs increase to $200 billion of Chinese products, as President Donald Trump has threatened. Those estimates don't factor in retaliation from China, which has vowed to match the U.S. dollar for dollar.

Balancing Act

China eased reserve requirements for some banks in order to stimulate lending, though some fear the move could exaccerbate China's already growing debt burden.



Source: Wind; Macquarie Group

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WSJ PRO CENTRAL BANKING

Economy

China Eases Policy | ECB Official: Late 2019 Discussion of Rate Rise | BOJ Concern Over Side-Effects | BIS: Disregard Market Volatility | Harrison's Take: Monetary Policy Divergence; The Wall Street Journal's central banking newsletter for Monday, June 25, 2018

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25 June 2018
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English

Harrison's Take: Monetary Policy Divergence Could Lead Investors to Look for Yield in the U.S.

China Eases Credit Policy as U.S. Tariffs Near

ECB Could Discuss Raising Rates From Autumn Next Year, Top Policy Maker Says

BOJ June Opinion Summary Shows Growing Concern Over Side-Effects of Easing

Central Bankers Should Disregard Volatile Markets, Says BIS

Monetary Policy Divergence Could Lead Investors to Look for Yield in the U.S.

We're entering into another period of monetary policy divergence.

In the U.S., Federal Reserve officials have made clear they intend to continue raising interest rates and have penciled in a full percentage-point increase in their benchmark rate over the course of 2018. The European Central Bank, meanwhile, has postponed a rate increase due to a recent spell of soft growth. The Bank of England also kept its benchmark rate on hold this week.

Although each central bank is responding to domestic economic circumstances, the moves can have a global impact.

When interest rate go up in one country and not in another, money tends to move toward the country with higher interest rates. In this case, we can expect to see money flowing into the U.S.

In particular, we can expect to see money flowing into U.S. corporate debt as investors search for yield, according to a new paper by economists at the Fed and the Bank for International Settlements. According to their research, when a country's interest rate falls by a percentage point, its investment in U.S. corporate bonds rises by 3.6% to 5.3% of gross domestic product. By contrast, its investment in Treasurys rises by only 0.2% of GDP.

That could mean more borrowing by U.S. firms.

And that could spell trouble. Fed Chairman Jerome Powell at his press conference following this month's policy meeting flagged the high levels of corporate debt as a cause for concern.

"That's really where leverage is at levels that are high relative to history," he said. "That's something we're watching very carefully."

As the gap in interest rates between the Fed and other major central banks widens, we could see corporate leverage increase. For now, Mr. Powell noted that defaults and interest rates remain low.

But it isn't hard to imagine a scenario in which rising rates put pressure on a lot of U.S. firms.

Key Developments Around the World

China Eases Credit Policy as U.S. Tariffs Near

China's central bank is freeing up more than $100 billion for commercial banks to boost lending and restructure debt, as the Chinese leadership tries to shore up growth amid slowing momentum for economic expansion and an intensifying trade brawl with the U.S. In a statement Sunday, the People's Bank of China announced that it is reducing the amount of reserves banks are required to keep with the central bank by half a percentage point starting July 5. That is the day before a U.S. deadline to slap punitive tariffs on tens of billions of dollars in Chinese goods.

Yuan's 2018 Gain Disappears as Dollar Rallies

ECB Could Discuss Raising Rates From Autumn Next Year, Top Policy Maker Says

European Central Bank officials could start to discuss raising short-term interest rates from autumn next year, a top ECB policy maker said, amplifying the caution expressed by the bank's President Mario Draghi in recent days. The ECB's patient approach comes as the 19-nation eurozone economy slows and faces burgeoning threats, including rising **oil prices** and escalating trade tensions between the world's biggest economic blocs.

BOJ June Opinion Summary Shows Growing Concern Over Side-Effects of Easing

A summary of opinions of the Bank of Japan's policy makers released Monday showed growing concern over the side effects of the bank's prolonged easy money campaign. One of the BOJ's nine policy board members said commercial banks faced growing unrealized investment losses and the risk of impairment losses at branches with low profitability, according to the summary of the board's June meeting. It is necessary to "consider the possible countermeasures against the side effects before they materialize," the member added.

Central Bankers Should Disregard **Volatile** Markets, Says BIS

Central bankers in the U.S. and Europe shouldn't be deterred from raising interest rates and winding back stimulus policies by the increased **financial market volatility** that will accompany their efforts, the Bank for International Settlements said Sunday. In its annual report, the club for central banks welcomed a series of rate increases by the Federal Reserve, as well as the European Central Bank's intention to halt purchases of government bonds in December.

Eurozone Gives Greece Some Debt Relief as Bailout Nears End

The eurozone agreed to lighten Greece's debt burden when the country's bailout ends this summer, but the measures fall short of what the International Monetary Fund and most economists say would be needed to end doubts about Greece's long-term solvency. The completion of the Greek bailout on Aug. 21 marks a symbolic end to the eurozone's long debt crisis, which put the survival of Europe's common currency in doubt earlier this decade. But the continued questions about whether Greece's debt is sustainable in the long run, and fresh worries about Italy's finances under its new populist government, show how far the eurozone remains from resolving its underlying problems.

Bank Indonesia Chief Reiterates Rate Rise to Be Considered at Next Meeting

Bank Indonesia Gov. Perry Warjiyo reiterated Friday that the central bank would consider raising interest rates next week to ensure stability in the local capital market. The statement was another indication the bank is likely to raise borrowing costs further as it now expects the U.S. Federal Reserve will raise interest rates four times this year instead of three, while the European Central Bank will start tapering its easy monetary policy in September. When a Bank Indonesia "governor says the measures to be taken could include a rate increase, the message is clear" that such measures most likely will be taken, Mr. Warjiyo said when asked about the probability of a rate increase.

Quick Hits: Bank of Canada Rate Rise Seen as Still 'Very Possible'

Soft inflation and retail sales readings in Canada raise questions about the central bank's policy path, and the Bank of England could raise rates in August even if economic data in the U.K. is underwhelming. Here are quick hits on central banking and related market views from around the world.

Monday

10 a.m. EDT

U.S. Commerce Department releases May new-home sales

12 p.m. EDT

San Francisco Fed's Gould (acting president) speaks

7:50 p.m. EDT

Bank of Japan releases May services PPI

9:20 p.m. EDT

ECB's Coeuré speaks

Tuesday

5:30 a.m. EDT

Bank of England's McCafferty speaks

1:15 p.m. EDT

Atlanta Fed's Bostic speaks

1:45 p.m. EDT

Dallas Fed's Kaplan speaks

7:50 p.m. EDT

Bank of Japan releases January-March flow of funds data

Regulatory Changes and the Cost of Capital for Banks

While "the cost of capital soared for banks in the financial crisis, after the passage of the Dodd-Frank Act, the value-weighted cost of capital for banks fell differentially more than did the cost of capital for nonbanks," Anna Kovner and Peter Van Tassel find in a Federal Reserve Bank of New York paper. "The very largest banks drive the decline in expected returns…We find some evidence that stress testing has lowered the cost of capital for the largest stress-tested banks, although not for those added more recently to stress testing," they write.

Goldman Sachs Shouldn't Be Able to Jawbone the Fed

"On Thursday evening, after the release of the first stage of the annual bank stress test, Goldman Sachs Group Inc. put out a statement indicating that it was unhappy with the results and said that it planned to air its grievances with the Federal Reserve. The bank said its estimate of how much it would lose in an economic downturn 'diverged' from the Fed," Stephen Gandel writes for Bloomberg View. "Another important point, however, is to gauge the risk controls of the banks to determine their proficiency at identifying those potential losses and estimating their size. If Goldman thinks it has a better idea than the Fed—which has looked into the books not only at Goldman but at all the banks—of how it will do in a downturn, that could be a problem. Having a divergence should result in more points being taking off, not fewer."

Americans entering retirement are in worse financial shape than the prior generation, for the first time since Harry Truman was president. This cohort should be on the cusp of their golden years. Instead, their median incomes including Social Security and retirement-fund receipts haven't risen in years, after having increased steadily from the 1950s.

Canada's annual inflation rate remained above 2% for a fourth straight month in May but came in well below market expectations, while measures of underlying price growth cooled slightly.

Reserve Bank of Australia Governor Philip Lowesucceeds William Dudley, the Federal Reserve Bank of New York's former president, as head of the Bank for International Settlements's Committee on the Global Financial System. The CGFS is a central bank forum for monitoring and analyzing developments that affect the stability of the financial system.

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

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

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Business News: U.S. Shale Motors Ahead Despite OPEC --- Producers should benefit from effort to keep high prices from hurting oil demand

By Rebecca Elliott and Christopher M. Matthews
783 words
25 June 2018
The Wall Street Journal
J
B3
English

U.S. shale companies, which profited by continuing to pump oil as the rest of the world cut its production, are again poised to benefit as the Organization of the Petroleum Exporting Countries boosts its output.

OPEC's decision last week to increase production modestly is seen as an attempt to keep prices elevated without creating a sharp rise. The move eased concerns among the member countries about tightening supply and the potential for a price increase, but it also lifted the stock prices of U.S. oil producers, which have learned to survive at whichever price OPEC pursues.

"We're not running our business based on what OPEC does regarding supply," said Doug Lawler, chief executive of Chesapeake Energy Corp., a pioneer of shale drilling. "We just have to respond accordingly and focus on the technology and the innovation that helps us be efficient regardless of the price."

U.S. production has grown at a record-setting pace this year, hitting 10.9 million barrels a day this month after **oil prices** exceeded $70 a barrel for the first time since 2014. That makes the U.S. the world's No. 2 oil producer behind Russia, but ahead of Saudi Arabia.

OPEC members, plus Russia, came to an agreement two years ago to cut production to shrink excess supply and prop up prices. At the meeting last week in Vienna, OPEC ministers cobbled together a deal to reverse course and boost oil output by an effective 600,000 barrels a day to head off a possible run to $100-a-barrel oil. Russia said over the weekend that it would support OPEC's efforts.

Speaking at the meeting in Vienna, Scott Sheffield, chairman of Pioneer Natural Resources Co., said the company has a shared interest with OPEC in preventing overheated prices. High prices generate a short burst of profits but can undermine economic growth and tamp down demand.

Mr. Sheffield said: "$100 is not going to help OPEC. It's not going to help us in the Permian." His company is one of the top drillers in the Permian Basin of West Texas and New Mexico.

OPEC's new barrels also come at an opportune time for shale companies, which are facing production-threatening infrastructure constraints in the Permian, the country's most active drilling region. Analysts say Permian producers might have to scale back drilling until new pipelines come online in 2019.

U.S. shale companies now have some breathing room, said R.T. Dukes, a director at the energy consulting firm Wood Mackenzie.

"It leads to a little bit lower price this year, but a little bit higher price next year because you have less spare capacity, less potential for OPEC to raise production," he said. "That'll be great timing for them as they'll be ramping up getting ready for those pipeline expansions to come online in the second half of the year."

OPEC's decision wasn't without drama, as Saudi Arabia pushed other member nations to agree to an increase after a contentious week of meetings. Members such as Iran, Venezuela and Libya approved the deal but have a limited ability to produce more oil themselves because of geopolitical concerns and production constraints.

Initially blindsided by the advent of fracking technology and U.S. production increases, OPEC allowed **oil prices** to nose-dive from more than $100 a barrel in 2014 to less than $30 a barrel two years later, an apparent attempt to force shale drillers out of business.

Hopes that falling prices would kill shale producers proved hollow. U.S. drilling dropped significantly, but oil production hasn't fallen below eight million barrels a day since November 2013, even as **oil prices** fell roughly 75% from 2014 to 2016. U.S. production had averaged about 5.5 million barrels a day from 2000 to 2012.

The tug of war over the global oil market left scars on both sides. Nearly 200,000 oil workers lost their jobs in the U.S., and OPEC eventually was forced to cut production. But U.S. producers used the downturn to become more efficient and have continued their production gains.

"The U.S. has broken OPEC's ability to totally control the market," said Ben "Bud" Brigham, who has made hundreds of millions of dollars as an oilman in shale plays in North Dakota and Texas. "We're their most significant competitor in terms of production."

Benoit Faucon contributed to this article.

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GE Nears $3 Billion Engine Sale --- Conglomerate to shed another industrial unit as it looks for cash; Advent is likely buyer

By Ben Dummett and Dana Mattioli
369 words
25 June 2018
The Wall Street Journal
J
B1
English

General Electric Co. is nearing a deal to sell a unit that makes large industrial engines to private-equity firm Advent International for $3 billion or more, people familiar with the matter said, a move that would bring in needed cash for the struggling conglomerate.

A deal, if completed, could be announced on Monday, the people said. Advent appears to have beaten out Cummins Inc. in an auction for the businesses, according to the people.

The sale is another step in Chief Executive John Flannery's push to simplify the beleaguered company after years of underperformance, by selling $20 billion worth of assets by the end of next year. GE last month agreed to sell its railroad division in a complex deal worth $11 billion.

But investors are waiting for a major portfolio update expected to come soon. Mr. Flannery continues to preach that "everything is on the table," including a breakup of the 126-year-old company.

GE just learned in recent days that it will be removed from the **Dow Jones Industrial Average** after more than a century in the blue-chip index. The company's shares closed Friday at $13.05, down by more than half in the past year.

The assets being sold are GE's so-called distributed-power business, which makes Jenbacher and Waukesha gas engines. These truck-sized machines, often painted bright orange or green, are used to generate electricity in remote areas, along with other industrial operations requiring a mechanical drive.

The deal unwinds two acquisitions by former CEO Jeff Immelt, who left last summer after 16 years at the helm. Mr. Immelt exited amid investor pressure to improve profits and revive the **stock price**, and following his departure GE slashed its dividend and financial targets.

GE acquired Jenbacher, based in Austria, in 2003. Waukesha, which dates back to 1906, came as a part of GE's purchase of oil-and-gas equipment maker Dresser Inc. for $3 billion in 2010.

Thomas Gryta contributed to this article.

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THE WALL STREET JOURNAL.

Markets

China, China, China: Beijing Cuts Reserves, but Investors Yawn; Asian stocks largely dropped on Monday

By Saumya Vaishampayan and Shen Hong
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25 June 2018
12:22 AM
The Wall Street Journal Online
WSJO
English

Asian stocks mostly fell on Monday, led by a 0.8% drop in Taiwan's Taiex index.

Monday's Big Theme

It's all about China, again. The People's Bank of China said Sunday it will cut the amount of reserves banks are required to keep with the central bank, which will free up more than $100 billion for commercial banks to boost lending and restructure debt.

What's Happening

The news is hitting the yuan, which is sliding against the dollar and has now erased its year-to-date gain, according to Wind Info.

One dollar bought 6.5301 yuan recently, which means the Chinese currency has lost 0.5% against the greenback for the day. It has now slipped 0.3% for the year.

But the central bank's announcement didn't boost the Shanghai Composite in a big way. The index flipped between slight gains and losses on Monday, rising 0.2% in recent trade. That's not much compared with how it reacted after the central bank made similar cuts in the past.

The Shanghai Composite rose 0.8% on April 18, the day after the PBOC said it planned to reduce the amount of reserves held by commercial banks.

The index also added 0.8% on Oct. 9, the first day of trading after the bank had announced a targeted required-reserves cut on Sept. 30. Chinese markets were closed for the local Golden Week holiday in between.

While the cut in banks' reserve requirement ratio should be positive for stocks, the prospect of a trade war with the U.S. and the slowing momentum of China's own economy continue to weigh on the market. In the latest sign of rising tensions, President Donald Trumpplans to bar many Chinese companies from investing in U.S. tech firms.

Market Reaction

"It's not so easy to rebuild confidence in a market which has just recorded a fresh two-year low and broken the key 3000 level it had tried to defend for half a year," said Zhang Yanbing, senior analyst at Zheshang Securities Co.

The Shanghai index has dropped for five straight weeks through Friday, putting it on the edge of a **bear market**. Despite the increasingly attractive valuations of Chinese stocks, "investors' sentiment remains quite weak at the moment," Mr. Zhang said.

Another reason why the central-bank news hasn't lifted stocks? "The PBOC did not surprise anyone," said Raymond Yeung, chief economist for greater China at ANZ in Hong Kong, pointing to a notice from the country's State Council last week flagging the move.

Ultimately, the central bank's latest credit easing may continue to have more of an impact on the yuan.

"The fact that the RRR cut came ahead of Trump's move slap additional tariffs on Chinese goods shows that the authorities are now willing to let the yuan slide a bit more," said a Shanghai-based senior currency trader at a mid-sized Chinese bank.

Elsewhere

Brent crude fell 1.8% on Monday, dwarfing the 0.3% pullback in U.S. **oil prices**. **Oil prices** rallied Friday after the some of the world's biggest oil producers agreed to boost crude output less than many investors had expected.

Lingling Wei and Chao Deng contributed to this article.

Write to Saumya Vaishampayan at saumya.vaishampayan@wsj.com and Shen Hong at hong.shen@wsj.com

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International New York Times

business
Italy’s Economy Was Humming Nicely. Then Came Trump.

By PETER S. GOODMAN
1,688 words
24 June 2018
International New York Times
INHT
English

GIOIA TAURO, Italy — From its headquarters in Calabria, the poorest, least-developed region in Italy, Gruppo Ventura looked out on the world and spotted a potentially lucrative growth opportunity — Iran.

The family-owned company installs railroad tracks. The Italian economy was sluggish, while Iran was poised to develop rapidly, having promised to abandon its pursuit of nuclear weapons in exchange for relief from crippling international sanctions.

The deal that Gruppo Ventura struck last year with an Iranian partner was modest, but the possibilities seemed big. Then, President Trump withdrew the United States from the Iran nuclear deal, dealing a blow to companies across Europe. A few weeks later, Mr. Trump imposed tariffs on steel and aluminum, provoking outrage among European allies, while threatening to make steel more expensive.

Along the way, the Italian political system served up the sort of agita-inducing drama for which it is rightfully famous, sowing worries that all of Europe could be vulnerable to a fresh crisis.

So much for Europe’s improved fortunes. So much for Gruppo Ventura’s international expansion.

“We were expecting to expand in Iran, build rails,” said Gruppo Ventura’s chief financial officer, Alessandro Ventura. “We are not expecting to do these things anymore.”

Across Europe — and especially within Italy — recent times have produced a series of bewildering, potentially expensive events that have conspired to replace a spirit of optimism with deepening concern.

Only a few months ago, Europe was the leading example of the vigor the global economy was gaining after the trauma of a world downturn. Even Italy, Europe’s traditional problem child, was growing.

But Mr. Trump’s decision to walk away from the Iran nuclear deal threatens to cost European companies billions of dollars in lost sales, with German, Italian and French players especially exposed. The reimposition of sanctions on Iran stands to limit the flow of its oil to world markets. This prospect has lifted fuel prices, applying pressure to European economies.

This month, Mr. Trump refused to spare Europe from his tariffs on steel and aluminum, then used an annual meeting of major democracies to double-down on his clash with allies, enhancing fears of trade conflict.

Gruppo Ventura presents itself as relatively insulated against such shocks, given that the Italian government pays it to service rail tracks — the sort of activity that must continue. Still, company executives are concerned that the cost of rail tracks will climb along with the price of steel.

“Everything is a bit more complicated,” said Gruppo Ventura’s chairwoman, Maria Antonietta Ventura.

All of this has been playing out against the latest outbreak of Italian political drama, which has placed power in the hands of two populist parties, the Five Star Movement and the League. They have promised to deliver tax cuts and a basic income program — unconditional cash grants for all — without elaborating on how they plan to pay for them, creating fresh worries about Italy’s alarming public debt. Their hostility toward the euro, the currency shared by 19 European nations, has reinvigorated concerns about its endurance.

This trifecta of troubles — higher **oil prices**, American steel tariffs and a crisis of confidence in the government — has turned Italy into a leading export of an unwanted commodity: worry.

“All three of those are going to have quite a big impact on sentiment this year, and probably add to quite a big slowdown,” said James Nixon, chief European economist at Oxford Economics in London. “It’s not a very pretty combination.”

On the afternoon when word broke that Mr. Trump would not exempt Europe from his metals tariffs, Claudio Capponi was struggling to calculate the impact.

He is the commercial director of IRON, a publicly traded company that makes industrial parts. Its factory sits in Assisi, in the central Italian province of Umbria. Until the moment that the American president rendered his decision, Mr. Capponi was confident the Continent would be spared.

“Europe is too good of a trade partner for the United States for President Trump to do this,” he said.

Giant coils of steel shipped from mills in France were spread across the concrete floors of his factory. As the sound of pounding metal echoed through the cavernous plant, machines sliced steel into customized shapes — arms for earth movers destined for the United States, silos to hold wind turbines, decks of cargo ships.

Given that IRON is a buyer of steel, the company might benefit from the American tariffs. Steel now shipped to the United States from mills within Europe might stay here to avoid the tariffs, raising the supply and lowering prices locally even as they increase in much of the world. Chinese producers that export to American shores could divert their product to Europe, amplifying this trend.

But Mr. Capponi was banking on none of this. Even if he pays less for steel, his customers are likely to squeeze him for lower prices. More broadly, the American tariffs — justified by the Trump administration as a defense of national security — reverberated as a blow against world trade.

“We depend on access to a global market,” Mr. Capponi said. “It’s the uncertainty that is driving us mad. We are looking out the window at what is going on outside of our factory. We’re worried about the precedent of these tariffs. We are worried the forces of protectionism are being set loose. The landscape is so unclear.”

Before the 1979 revolution in Iran, Italian companies were key players there, building a port at Bandar Abbas, on the Persian Gulf. After the revolution, and before the advent of international sanctions, Italian energy and construction companies were a significant presence.

Once the Obama administration and leaders of other world powers struck the nuclear deal with Iran three years ago, Italy saw a chance to reclaim its perch. Iran was a land of 80 million people in need of upgrades to its electrical grid, its ports, its transportation systems.

Last year, Italy exported more than 1.7 billion euros (nearly $2 billion) worth of goods to Iran, up from €1.2 billion in 2015, according to the European Union. Only Germany exported more, sending nearly €3 billion worth of goods to Iran.

Invitalia, an Italian government agency that promotes trading opportunities, created a company focused on expanding investment in Iran. The new entity was authorized to provide loan guarantees to support Italian ventures in Iran.

Invitalia was soon inundated with proposals from Italian companies. The agency was mulling which to back when the United States announced the resumption of Iran sanctions, asserting this would pressure Tehran to curb its support for terrorism and its development of advanced missiles. The Trump adminstration gave companies three to six months to wrap up activities there.

“This project is on pause,” said Domenico Arcuri, chief executive officer of Invitalia. “We are waiting for the situation between the United States, Europe and Iran to be clarified. In this condition, these projects will be suspended for a long time.”

American sanctions not only bar domestic companies from doing business in Iran but also threaten foreign businesses with being frozen out of the American financial system. Given that the American dollar remains the dominant means of global exchange, that prospect has halted most transactions.

Before Mr. Trump’s decision, Giorgio Meniconi, owner of a small factory in Tuscany, was preparing plans to expand in Iran. His company, Tecon, makes a tool used to slice leather into shoes, jackets and bags.

For years, counterfeit versions of his product have circulated in Iran, the handiwork of Chinese factories. He took the nuclear deal as impetus to register his company trademark in Iran and forge a relationship with a local distributor.

But last month, the distributor called and canceled the deal. Since Mr. Trump opted to reinstate sanctions, Iran's currency has plunged against the euro, making Tecon's products too expensive.

"I had great hopes for Iran, because I saw it as a gateway to other markets in central Asia," Mr. Meniconi said. "The hopes we were building were shattered."

In the years before Gruppo Ventura secured its Iran venture, Mr. Ventura traveled there some 20 times. In March 2017, he signed a €2 million contract (about $2.3 million) to service a section of rail outside Tehran.

He shipped two locomotives used to tamp down the rocks below railroad tracks. They went out on a freighter from Gioia Tauro, a port on the Tyrrhenian Sea that has long been notorious as a Mafia-run conduit for cocaine trafficking.

In August, Mr. Ventura stood at the Iranian port of Bandar Abbas in 122-degree heat, watching a crane hoist the locomotives onto the docks.

Now, those machines are effectively marooned, the business halted. Gruppo Ventura has lost its appetite for adventurous expansion.

"We are wary of going into markets that America dislikes, because we never know what they will say," said Ms. Ventura, the chairwoman.

Five company technicians dispatched to Iran to maintain the locomotives have returned here, to the company's warehouse.

"It was a beautiful thing that our company would go," the head mechanic, Renato Tocci, said. "Our hope was that our business would grow. Now, it's a time where everything is stalled."

PHOTOS: A factory in Assisi, Italy, run by IRON. "We depend on access to a global market," said Claudio Capponi, a company official. (BU1); Gruppo Ventura, which installs railroad tracks, is led by Alessandro Ventura, left, its chief financial officer, and Maria Antonietta Ventura, its chairwoman and his sister. Gruppo Ventura also performs maintenance on locomotives. The company is worried that the cost of tracks will climb along with the price of steel. "Everything is a bit more complicated," Ms. Ventura said. Below, Claudio Capponi, a company official. (PHOTOGRAPHS BY GIANNI CIPRIANO FOR THE NEW YORK TIMES) (BU6)

* Just the Fear of a Trade War Is Straining the Global Economy

* For Europe, an Unpleasant Question: Confront Trump or Avoid a Costly Trade War

* Italy Is Having an Election. Most Italians Are Too Depressed to Care.

Document INHT000020180626ee6o0000f

THE WALL STREET JOURNAL.

Markets
Why $39 Billion of Stocks Traded in One Second on Friday; This year's rebalancing of FTSE Russell's indexes affected billions of dollars

By Asjylyn Loder
827 words
24 June 2018
The Wall Street Journal Online
WSJO
English

Corrections & Amplifications

A record 1.2 billion shares worth more than $39 billion traded in less than a second on Friday during **Nasdaq**'s closing auction. An earlier version of this article incorrectly said 1.2 million. (June 25, 2018)

A record 1.2 billion shares worth more than $39 billion traded in less than a second on Friday during **Nasdaq**'s closing auction. The reason: the end of this year's rebalancing of FTSE Russell's widely followed stock indexes.

There are $9.2 trillion pegged to Russell U.S. benchmarks, dwarfing the $29.5 billion linked to the **Dow Jones Industrial Average**, which made headlines last week by ejectingGeneral Electric Co. after more than a century.

When Russell adds and removes stocks each year to and from its indexes, stocks that are part of the revisions typically experience a trading volume spike 45 times higher than average, according to research from Keefe, Bruyette & Woods. This year, nearly 300 companies were added or dropped from the Russell 2000 alone.

Getting added to a prominent benchmark is akin to gliding past Wall Street's velvet ropes, a big boost for firms that otherwise hover beneath Wall Street's radar. Walgreens Boots Alliance Inc. climbed 4.6% following the June 19 announcement that it would replace GE in the Dow, even as the index remained flat. For lesser-known firms, winning a coveted spot in the Russell 2000, a popular index of small companies, helps them win the attention of investors.

"You're suddenly attractive to all of these investors that couldn't buy your stock before because you weren't in their benchmark," said Melissa Roberts, head of quantitative research at Keefe, Bruyette & Woods, a New York investment bank.

The spike in trading activity underscores how index companies have morphed into some of Wall Street's most powerful stock pickers. Investors have forsaken active money managers in favor of low-cost passive investments, so when major market benchmarks rearrange their lineups, those changes reverberate throughout the **stock market**.

The jockeying was evident last month as traders bid up shares of First United Corp. in an effort to push its market value above the $159.2 million threshold for inclusion in the Russell 2000, a popular index of small companies, Ms. Roberts said.

First United's market capitalization was $132 million on May 9, two days before the deadline to win a spot in the index. Over the next two days, its share price rocketed up 20%. By the time the closing bell rang on May 11, First United's market value had risen to $159.37 million, making it one of the smallest new entrants to the index.

"There was a lot of interest there in making sure this company made it in," Ms. Roberts said.

Investors say First United announced stellar first-quarter results on May 9. But professional traders build models designed to predict who will make the cut on deadline day, and the prospect of getting into the Russell had an "accelerating effect" on First United, Ms. Roberts said.

This isn't a new phenomenon. Ever since index investing emerged in the 1970s, Wall Street has made a cottage industry of betting against it. The annual rejiggering of the Russell indexes is unusually easy to predict, even in the world of plain-vanilla benchmarks, Ms. Roberts said. Firms such as Barclays PLC have become well-known Russell forecasters, and traders start placing their wagers on the changes months in advance.

"These are all signs of a transparent and efficient market, and it helps keep markets orderly as opposed to a surprise," said Rolf Agather, a managing director at FTSE Russell, a subsidiary of London Stock Exchange Group. He also pointed out that FTSE Russell has altered its methodology over the years reduce turnover, which makes it tougher for traders to front-run their indexes.

Critics say all that speculation can inflate the prices of potential new additions and drag down the stocks that are being removed. Earlier this month, acclaimed investor Rob Arnott, the founder of Research Affiliates, said fund managers who slavishly mimic their index end up buying high and selling low, a hidden cost that erodes returns over time.

The picture isn't one-sided, Ms. Roberts said. Come rebalance day, passive investors need to buy and sell big blocks of thinly traded shares, and the traders who jumped ahead of the index, will supply much-needed inventory. Passive index-tracking funds had $57 billion of trading to do after Friday's closing bell to get ready for Monday's changeover, she said.

Betting against the Russell also isn't a guaranteed win, said Jared Dillian, investment strategist with research firm Mauldin Economics. Traders aren't just wagering against the index. They also must outwit each other.

"You're in this trade with a bunch of other banks and hedge funds," Mr. Dillian said. "But at some point you have to get out."

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THE WALL STREET JOURNAL.

Markets

How One Small School's Endowment Is Topping the Class; Quinnipiac University of Connecticut has beat peers by investing in stock pickers—and sticking with them

By Dawn Lim
985 words
24 June 2018
08:00 AM
The Wall Street Journal Online
WSJO
English

Quinnipiac University, a small school best known for political polls, is beating the biggest names in higher education at investing with the help of an unlikely force: the stock picker.

The private university tucked away in the Connecticut hills delivered annualized gains of 6.1% for the decade ended June 30, 2017. The returns are in the top 10% of U.S. schools ranked by the National Association of College and University Business Officers and Commonfund.

John Lahey and Mark Varholak, the two university administrators overseeing the roughly $530 million endowment, say the school has steered clear of the crush of investors into index funds and big private-equity bets.

Instead, it achieved its stellar returns by investing 70% of its money with stock pickers and sticking with them.

Quinnipiac tapped one of its top managers, an obscure equities shop named Greenhaven Associates, in the 1990s. The Purchase, N.Y., firm, closed to new investors for a decade, now manages nearly a fifth of Quinnipiac's endowment. It delivered average annual returns of 17.1% before fees for the school between early 1999 and 2017, said people familiar with the matter, far in excess of the **S&P 500**.

"We know equities," said Mr. Lahey, the university's 71-year-old president, who plans to teach philosophy after he retires in June following more than three decades at the helm. In contrast to more complex investments, in stocks "there's more transparency," he said.

The approach Mr. Lahey champions muddies the playbook for U.S. colleges seeking to grow their wealth and have more money to spend on attracting students.

Many investors have abandoned stock pickers as the U.S. **stock market** shrinks and money surges into low-cost indexes. The average actively managed fund focused on U.S. stocks lagged behind the **S&P 500** in the decade ended June 30, according to Morningstar data.

Quinnipiac, in contrast, has no money in index funds and stayed with stock pickers for the long haul.

Greenhaven began in the 1980s as an investment arm of a family office. Founded by value investor Edgar Wachenheim, the $7 billion-plus firm is risk averse, deliberately aiming not to beat benchmarks. It seeks investments in companies with strong balance sheets that will benefit from changes the market overlooks.

Among Greenhaven's current investments are banks including Citigroup Inc., auto makers such as General Motors Co. and home builders.

Many college endowments build complex portfolios managed by a swarm of managers. Greenhaven is one of the handful of equity managers investing Quinnipiac's money.

"It's my job to resist the proliferation that ends up with mediocrity," said William Spears, a co-founder of wealth manager Spears Abacus who chairs Quinnipiac's investment committee. He asked Mr. Wachenheim to manage the school's money about two decades ago.

Quinnipiac, founded during the Great Depression, has a rising enrollment rate that surpassed 10,000 students in the past school year. Unlike many of its peers, the school doesn't rely on its endowment for any operating needs and plans not to spend from the pool until it hits $1 billion.

With no dedicated chief investment officer, Quinnipiac still bested every Ivy League college with returns of 20.9% in fiscal 2017. Yale University posted returns of 11.3% and Harvard University8.1%.

The university never felt the pressure to copy the model pioneered by Yale investment chief David Swensen that pushed many college endowments to invest heavily in alternative and illiquid strategies such as private equity and venture capital.

The school, recognizing it doesn't have the same access to top buyout and venture managers as larger colleges, earmarks just 20% of assets split between hedge funds and private investments.

"They are aware of what other Ivies are doing and don't let others affect their thinking," said Peter Dunne, a managing director at a Bank of America Merrill Lynch institutional consulting group advising Quinnipiac.

The university takes comfort that about 80% of its assets can be converted to cash in 30 days. "Even with a long-term value tilt, the equity managers have created a highly liquid endowment," said Mr. Varholak, Quinnipiac's chief financial officer.

The financial crisis vindicated its approach. Like other schools, Quinnipiac's endowment lost money in the 2008 credit crisis. But it recovered to its 2007 level by the end of 2009. Yale and Harvard took about seven years to return to their 2007 sizes partly because they were spending endowment money.

After the fall of Lehman Brothers, Quinnipiac didn't change its investment mix and proceeded with plans to expand its graduate campus and build new dorms. "I may have lost a little sleep and needed an Irish whiskey here and there," said Mr. Lahey, a second-generation Irish-American who has marched in every annual New York City St. Patrick's Day parade for the last 38 years. "But we had ambitious plans and didn't get weak knees."

Some committee members have told university officials they hope the endowment's strategy won't change dramatically once Mr. Lahey leaves and Judy Olian, dean of the UCLA Anderson School of Management, takes over. "We are lucky to have continuity we have had," Mr. Spears said.

Mr. Lahey isn't blind to the uncertainty ahead once a **bull market**—now in its ninth year—runs out of steam. It isn't clear if the college will be better protected than others in another downturn. And the university concedes Yale beat out Quinnipiac in the last decade: 6.6% to 6.1%.

"I'm still a huge fan of David Swensen," Mr. Lahey said.

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THE WALL STREET JOURNAL.

Economy

Central Bankers Should Disregard Volatile Markets, Says BIS; The Bank for International Settlements also warns that increased sales of Treasury bonds by the U.S. government could slow the global economic expansion

By Paul Hannon
536 words
24 June 2018
06:30 AM
The Wall Street Journal Online
WSJO
English

Central bankers in the U.S. and Europe shouldn't be deterred from raising interest rates and winding back stimulus policies by the increased **financial market volatility** that will accompany their efforts, the Bank for International Settlements said Sunday.

In its annual report, the club for central banks welcomed a series of rate increases by the Federal Reserve, as well as the European Central Bank's intention to halt purchases of government bonds in December.

It urged policy makers to continue on the path of "normalization" even if that triggers sharper prices moves in financial assets, including those based in emerging markets. Indeed, the BIS said such **volatility** would be welcome if it made investors more cautious.

"Policy makers will need to maintain a steady hand, avoiding the risk of overreacting to transitory bouts of **volatility**," the BIS said. "Higher **volatility** per se is not a problem as long as it remains contained; it is actually healthy whenever it helps inhibit unbridled risk-taking."

The BIS also urged governments to cut back on their borrowings and said increased sales of Treasury bonds by the U.S. government could slow the global economic expansion.

The prospect of further rate rises by the Fed in 2018 has weakened some emerging markets currencies as investors shift their money into U.S. assets. However, the BIS said the Fed should not be deterred by those moves and that governments in emerging markets should do more to cushion themselves against the impact of capital outflows.

"This calls for other countries, in particular emerging markets countries, to strengthen their macro frameworks, and if possible to implement macroprudential policies to smooth the impact of this normalization," said Agustín Carstens, the BIS's general manager and formerly the governor of the Bank of Mexico.

Mr. Carstens said the long period of stimulative policies had created a number of "vulnerabilities," including "elevated" prices for shares and homes that have been fueled in part by increased borrowing.

"In previous episodes, such vulnerabilities have heralded a range of problems, including recessions," he said, according to the text of a speech to central bankers gathered in Basel, Switzerland for their annual meeting.

While welcoming the Fed's moves, the BIS highlighted U.S. government actions that could threaten the global economic recovery. In particular, it cited the dangers of a widening trade conflict and increased borrowing to fund tax cuts and increased spending.

"One possible trigger of an economic slowdown or downturn could be an escalation of protectionist measures," it said. "A second possible trigger could be a sudden decompression of historically low bond yields or snapback in core sovereign market yields, notably in the United States. The prospective heavy issuance of government debt…could add to this risk."

The BIS said that governments shouldn't be providing additional stimulus to economies that are already growing and should instead be cutting back on their debts.

"With due regard for country-specific circumstances, fiscal consolidation is a priority," it said.

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The New York Times

Business/Financial Desk; SECTB
Relief Buoys Energy Stocks After OPEC Decides to Increase Production

By THE ASSOCIATED PRESS
872 words
23 June 2018
The New York Times
NYTF
Late Edition - Final
6
English

Shares of **oil prices** and energy companies rallied on Friday after OPEC said it would produce more oil, but not as much as investors feared. While trade tensions remained in the headlines, United States stocks finished slightly higher at the end of a bumpy week.

Crude oil futures jumped 4.6 percent after the Organization of the Petroleum Exporting Countries agreed to produce about 1 million additional barrels of oil per day. Investors have expected an increase in production for weeks and many of them thought a bigger increase was coming, which would have sent prices lower. Shares of health care and household goods companies also rose while technology companies and banks fell. The **Dow Jonesindustrial average** broke an eight-day losing streak.

While prices usually go down when oil production rises, investors thought OPEC might take a bigger step based on reports over the last few weeks.

''People were pricing crude in the last couple of weeks (expecting) a bigger increase by OPEC than what they agreed to,'' said Jim Paulsen, chief investment strategist for the Leuthold Group .

The European Union followed through on its promise to put import taxes on $3.4 billion worth of American goods, including bourbon, peanut butter and orange juice, in response to United States tariffs on steel and aluminum. Automakers were jolted after President Donald Trump threatened to put a 20 percent tax on cars imported from Europe, although none of them took big losses in the markets on Friday.

The **Standard & Poor's 500**-**stockindex** added 5.12 points, or 0.2 percent, to 2,754.88. The Dow gained 119.19 points, or 0.5 percent, to 24,580.89. The Dow lost 2 percent this week, with Boeing shares off 5.3 percent and Caterpillar stock down 6.7 percent. That was both companies' biggest loss in three months. Makers of chemicals and other basic materials like 3M also lost ground this week and shares of technology companies slipped.

The **Nasdaq composite** fell 20.13 points, or 0.3 percent, to 7,692.82. The Russell 2000 index of smaller-company stocks sank 3.37 points, or 0.2 percent, to 1,685.58.

United States crude climbed 4.6 percent to $68.58 a barrel in New York. That was its biggest one-day gain since November 2016, when OPEC and a group of other countries including Russia agreed to cut production by 1.8 million barrels a day.

Brent crude, the standard for international **oil prices**, rose 3.4 percent to $75.55 a barrel in London.

Exxon Mobil stock picked up 2.1 percent to $81.38 and Marathon Oil shares surged 7.8 percent to $21.48.

On Twitter , Trump threatened to impose a 20 percent tax on cars imported from the European Union if barriers to trade were not removed soon. He previously ordered the United States trade representative to look into possible tariffs or quotas on imported cars and car parts.

That jolted car companies. In Germany, shares of BMW lost 1.1 percent and Daimler stock sank 0.3 percent. Daimler stock fell more than 4 percent on Thursday after it said Chinese tariffs on American cars would contribute to a decline in its earnings this year. Shares of Ford and Toyota also dipped while Peugeot and General Motors stock rose.

"If you're in the direct line of fire from a tariff, it's hugely important," Mr. Paulsen said. Still, he said, investors were very skeptical that a damaging trade war would break out. "The trade war has heated up over the last couple of months and yet stocks are up over that period of time," he said. That was also the case Friday.

Shares of the open source software maker Red Hat dropped 12.4 percent to $142.14 after it cut its sales forecasts because of the strengthening dollar. Shares of other technology companies also declined. The industry has been leading the market for more than a year, but it makes more of its sales outside the United States than any other major **S**.**&P**. **500** group. Micron Technology stock fell 3.9 percent to $57.10 and Nvidia stock lost 2.4 percent to $250.95.

Gold rose 0.2 percent to $1,270.20 an ounce.

Bond prices were little changed. The yield on the **10**-**year Treasury** note stayed at 2.90 percent.

The dollar edged down to 109.96 yen from 109.98 yen. The euro advanced to $1.1657 from $1.1611.

The CAC-40 in France climbed 1.3 percent and in Britain, the FTSE 100 gained 1.7 percent. In Germany, the DAX rose 0.5 percent.

Some Asian markets rose after heavy losses on previous days but finished lower than a week ago. In Hong Kong, the Hang Seng index edged up 0.2 percent while the Nikkei 225 in Japan lost 0.8 percent. The Kospi in South Korea advanced 0.8 percent.

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 --- Heard on the Street -- Beijing's Challenge: Propping Up Stocks --- Can government stop selloff without stirring panic?

By Jacky Wong
366 words
23 June 2018
The Wall Street Journal
J
B14
English

[Financial Analysis and Commentary]

Chinese stocks are almost in a **bear market**. That's leaving Beijing in a pickle.

Shanghai's main benchmark closed Friday nearly 20% down from its most recent high, set in January. Worries about escalating U.S.-China trade tensions sent the index down 4% this past week alone.

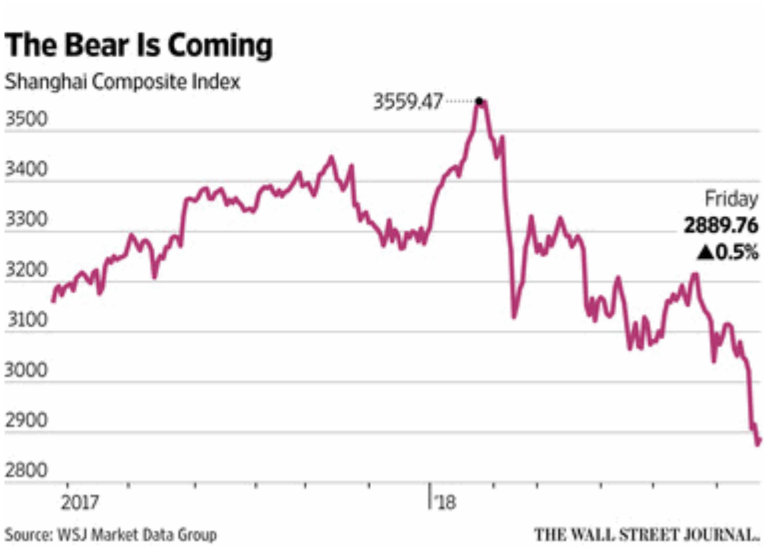
The trade-war rhetoric is just pushing Chinese stocks further in the direction they were already headed. Regulators have been trying to rein in China's monster shadow banking system for several months, cracking down on the proliferation of wealth-management products. This, along with rising wholesale borrowing costs, has dried up some of the liquidity that had been underpinning stocks.

So far, Beijing hasn't carried out a big rescue effort, as it did in the summer of 2015 when the market lost a third of its value in just a month. Partly, that's because this year's move has been more gradual.

It's also because the government has never quite left the market anyway. The so-called national team, an assortment of government-backed investment funds that often acts to stabilize the market, still owns nearly half a trillion dollars of stocks, according to Wind Information.

Beijing is now in a delicate position, as it decides whether to step up its efforts. One big risk is the fact that major shareholders of listed companies have pledged more than $800 billion of stocks in return for loans, according to data from the China Securities Depository and Clearing Corp. Any sudden sharp drop in the **stock market** from here could trigger margin calls, which could snowball into more stock selling.

Little wonder, then, that market participants are expecting some action in the coming days. A cut in the reserves that banks are required to hold at the central bank, which help increase liquidity, seems likely. Beijing will want to ensure this isn't taken as a sign of panic. But beneath the calm surface, policy makers are paddling ever harder.



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THE WALL STREET JOURNAL.
U.S. EDITION

EXCHANGE --- Finance: Don't Discount The Dow's Discards --- General Electric is down and out, but stocks removed from the index tend to outperform its new entrants

By Ben Eisen
382 words
23 June 2018
The Wall Street Journal
J
B8
English

General Electric Co.'s removal from the **Dow Jones Industrial Average** this past week was a new low for the struggling industrial giant. But it could also be a sign of brighter days ahead.

GE will no longer be part of the blue-chip index come Tuesday, after the committee tasked with selecting Dow components decreed that it will be replaced by Walgreens Boots Alliance Inc. Over the past 12 months, GE has fallen 53% as it struggled to reorganize its business, minimizing the firm's influence in the price-weighted index.

In the past, getting kicked out of the Dow hasn't been as bad for a stock as might be expected. The last 10 booted companies have risen an average of 6.4% in the year after their respective removals, according to The Wall Street Journal's Market Data Group. The past 10 additions, by contrast, have fallen an average of 4.6%. (Wall Street Journal editors are included on the committee that makes decisions about Dow components.)

For GE, once among America's biggest companies, the removal caps its lengthy decline. The company failed to grow its sprawling operation in recent years even as the broader economy recovered from the financial crisis. And critics say the company masked the extent of its troubles under former Chief Executive Jeffrey Immelt.

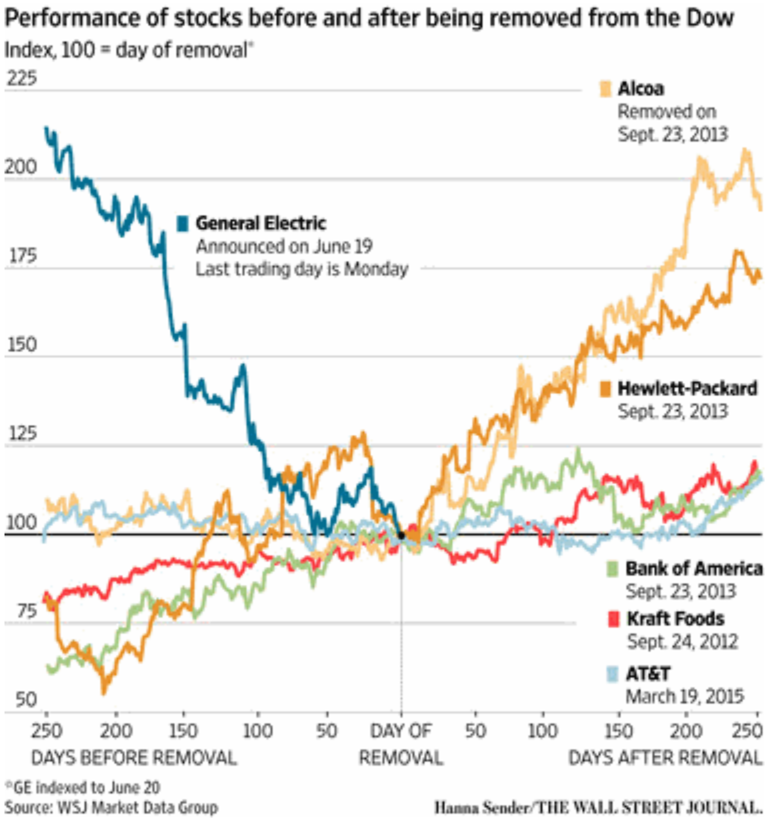
But there's a possibility GE's exit from the index could be happening right as it's hitting rock bottom. Analysts are predicting GE shares will rise, with the mean price target for the stock clocking in at $16.42, according to FactSet, 26% above its current price.

"The damage has already been done," said Brad McMillan, the chief investment officer at Commonwealth Financial Network.

New CEO John Flannery has been cutting jobs and trimming costs. The company plans to jettison $20 billion worth of its assets by the end of 2019.

It's too soon to know which way GE's shares will go. But history suggests investors shouldn't count out the Dow's discards.

Akane Otani contributed to this article.



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THE WALL STREET JOURNAL.
U.S. EDITION

Oil Soars As OPEC Agrees to Small Boost

By Benoit Faucon and Summer Said in Vienna and Stephanie Yang in New York
1,064 words
23 June 2018
The Wall Street Journal
J
A1
English

Oil prices rose by the biggest amount in nearly two years Friday after some of the world's major oil producers agreed to boost crude output less than many investors had feared.

Ministers from the Organization of the Petroleum Exporting Countries ended a contentious gathering with a loose promise to boost output by about 600,000 barrels a day. That was far less than the one million barrels many predicted.

The result dashed the hopes of some big producing nations like Russia, which wanted to raise production further to sell more crude at these higher prices. The move was cheered by investors, who say they now feel more confident the global glut that dragged U.S. **oil prices** below $30 a barrel isn't about to return.

U.S. **oil prices** surged 4.6% to $68.58 a barrel; the price of Brent, the international benchmark, rose $2.50, or 3.4%, to $75.55. For U.S. prices, it marked the biggest one-day jump since November 2016 when OPEC agreed to cut oil output for the first time in eight years.

Oil prices have risen briskly this year amid improving global economic growth and unexpected supply outages, drawing complaints from big consuming countries, like the U.S.

OPEC said Friday its members had tentatively agreed with their non-OPEC partners to end their overcompliance with production curbs they set in 2016 to add barrels to the market.

On paper, such a move would add about one million barrels a day to global markets, officials said. But the boost is to be shared among all members, some of whom can't raise output at all right now. That translates into about 600,000 barrels of new oil a day, said people familiar with the deal's technical aspects.

The 2016 cuts had helped boost **oil prices** to a 3 1/2-year high earlier this year, sending U.S. crude prices above $70 a barrel and boosting the earnings of big global producers like Exxon Mobil Corp. and Chevron Corp.

But pressure from Washington and big consuming countries, as well as concerns that prices rising too quickly could curb consumer demand, prompted OPEC on Friday to release more supply.

"This OPEC decision was a big uncertainty," said Adam Rozencwajg, managing partner at Goehring & Rozencwajg Associates. "Now that it is behind us, the **bullish** supply and demand fundamentals can once again come to the fore."

Since the November 2016 agreement, global inventories have drawn down to the five-year average and hit the lowest level in three years this year, according to the International Energy Agency. OPEC's efforts have been aided by strong global growth and demand for fuel, as well as unexpected supply disruptions.

Crude stockpiles in the U.S. have also declined steadily, which is part of the reason U.S. prices had such a strong reaction Friday. "The market was drawing inventories, we had seen a tight balance, and OPEC needed to increase supplies to address it," said Greg Sharenow, portfolio manager at Pacific Investment Management Co. "Now the concern in the market will pivot to, 'Where is the excess capacity in the system?'"

Even as shale production has climbed to record levels, data from the U.S. Energy Information Administration this week showed domestic inventories had fallen the lowest level since March. On Friday, oil services firm Baker Hughes Inc. also released weekly data showing the number of rigs drilling for oil in the U.S. declined -- a bellwether for the sector's activity.

"The first story is the resolution of the OPEC meeting and everyone going back about their business," said Mark Benigno, director of energy trading at INTL FCStone. "And the second is a squeeze going on in the physical side."

The deal still needs final, official approval from Russia and its non-OPEC partners. OPEC and that group are set to meet on Saturday. Russia has been heavily involved behind the scenes in hammering out the contours of a Friday deal with Saudi Arabia. One person familiar with the matter said Saturday's meeting was widely expected to certify the deal.

The group had agreed two years ago to reduce global output by 2%, or about 1.8 million barrels a day. Skeptics doubted whether oil producers could achieve their goal because such accords are hard to monitor and enforce. For governments, holding back barrels means forgoing revenue.

Eventually, though, the pact succeeded in whittling down the excess inventories of stored oil that developed nations had stockpiled and boosted prices. President Donald Trump has complained -- tweeting about prices being too high and blaming OPEC.

On Friday, he reengaged, tweeting shortly after the OPEC meeting finished his hope the cartel "will increase output substantially. Need to keep prices down!"

U.S. officials also asked Saudi Arabia, OPEC's de facto leader, to open up the taps to cushion the blow from Washington's fresh sanctions on Iran earlier this year, according to people familiar with the matter.

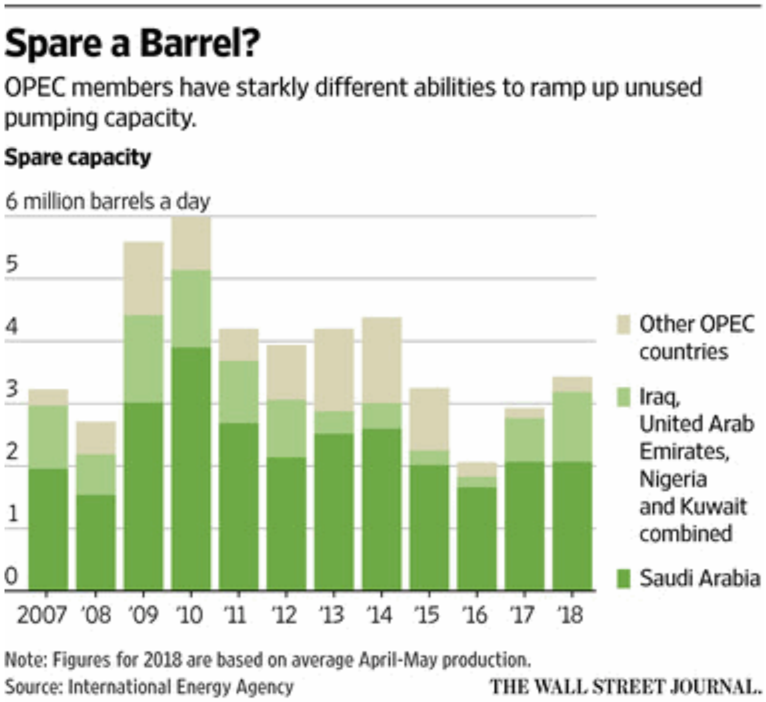
OPEC members themselves have long been sensitive to how high prices can soften demand by encouraging conservation and other energy sources like renewables, spiraling into a fresh glut and lower prices.

Russia, meanwhile, a key partner in OPEC's pact, has pushed to raise production. A contingent of private oil companies make up a good chunk of the country's output, and they have lobbied Moscow to let them pump more.

Saudi Arabia has been a proponent of keeping output in check. It and some of its Persian Gulf allies inside OPEC initially pushed for a very small boost -- well under 500,000 barrels a day. OPEC member Iran, meanwhile, opposed any cut.

Iran accused its regional rival Saudi Arabia of doing the U.S.'s bidding. Iran also worried that if others boost output, they might steal its market share. Several times during the week, Iranian Oil Minister Bijan Zanganeh threatened to pull out of any OPEC deal to hike output. Early Friday, he and Saudi Energy Minister Khalid al-Falih spoke to help smooth over differences.

Iran ultimately agreed, winning a promise that OPEC wouldn't provide any concrete numbers to its deal, said people familiar with the matter.



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The New York Times

Business/Financial Desk; SECTB

OPEC, After Bolstering Prices, Agrees to Ramp Up Oil Output

By STANLEY REED; Clifford Krauss contributed reporting from Houston.
1,217 words
23 June 2018
The New York Times
NYTF
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2
English

VIENNA -- Major oil-producing countries agreed on Friday to jointly raise exports, a decision that has driven considerable division among them but could temper criticism from President Trump.

Officials from the Organization of the Petroleum Exporting Countries, as well as other major producers like Russia, were set to increase their total output by around 1 percent of the global oil supply. Though a relatively small addition to the world energy market, the move nevertheless signals a willingness by international suppliers to address rising prices.

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The deal to cut output, reached in 2016, had been an extraordinarily cooperative effort by OPEC and other producers. Countries that had historically been at odds agreed to restrict their overall crude sales to bolster prices, with Saudi Arabia and Russia holding back the most.

But the curbs have generated opposition among major oil consumers. Mr. Trump, perhaps with an eye on the midterm elections in November, has repeatedly criticized OPEC for maintaining what he said were ''artificially very high'' prices, while other major oil importers like India have also been critical. The president weighed in on Friday, saying in a tweet that OPEC would need to ''increase output substantially.''

Saudi Arabia, OPEC's de facto leader and a major American ally, has pushed for a change in course. The country is an oil-producing juggernaut and has the spare capacity to quickly raise production. But others, particularly Riyadh's regional rival Iran, have pushed back.

Iran is already exporting oil at close to its maximum capacity, and so will not be able to take advantage of the increase. In fact, the country would be likely to suffer because the increased supply would force prices lower, reducing Tehran's government revenues. The timing is far from ideal for Iran, which is having to grapple with the possible impact of American sanctions on its energy sector.

The tensions have been evident here in Vienna. Iran's oil minister, Bijan Zanganeh, stormed out of a preparatory technical meeting on Thursday, frustrated by what he saw as Saudi Arabia forcing through its proposals.

Saudi Arabia has gone from being a price hawk, wary of raising production to alleviate increasing **oil prices**, to a dove. On Thursday, Mr. Falih told his colleagues at a seminar in Vienna that there could be a supply shortfall of 1.6 million to 1.8 million barrels a day of oil later this year, making a reversal of the cuts imperative.

''We are not going to allow a shortage to materialize to the point where markets will be squeezed and consumers will be hurt,'' he said.

While he vowed to be ''sensitive'' to the concerns of producer countries like Iran and Venezuela that are unlikely to be able to raise output and benefit from increased production, he made clear that Saudi Arabia was determined to increase supplies.

Mr. Falih said he hoped to keep the group together, and to work in unison to head off extremes like prices that topped $100 a barrel in 2014, only to be followed by a sudden crash.

''One thing you can be assured of is, we will be responsive,'' he added. ''We will release supplies.''

OPEC members said they would collectively adhere to production levels originally agreed to in 2016. Other producers like Russia are expected to reach a similar arrangement on Saturday. In total, the deals equate to a likely production increase of as much as 1 million barrels a day.

To avoid internal friction, however, the group did not allocate individual quotas, according to Suhail Mohamed Faraj al-Mazrouei, the energy minister of the United Arab Emirates, who was presiding over the OPEC meeting.

Analysts said that fuzzy math and a lack of quotas for specific countries could lead producers with spare capacity, like Saudi Arabia and Kuwait, to let output rip.

''As the months progress, compliance will come off, and countries will take advantage,'' said Abhishek Deshpande, an analyst at J.P. Morgan.

The prospect of increased supplies -- Russia and Saudi Arabia had proposed the outlines of Thursday's deal last month -- has helped cool off what had been fast-rising prices. What happens to those prices now may depend on factors that are out of OPEC's control. Among them are the possible impact of American sanctions on Iran's oil sector, and the continuing collapse of Venezuela's oil industry, as well as the consequences of a widening array of trade disputes on economic growth and demand for oil.

The changing American role in world energy markets is itself a variable. While Mr. Trump is leaning on OPEC to keep gasoline prices down, the United States is on the verge of becoming the world's largest oil producer, as well as a major exporter of both oil and gas.

''I think this rearranges the mental geography of the global oil market and, really, geopolitics,'' said Daniel Yergin, an oil historian observing the OPEC meeting in Vienna.

The transformation of the American oil industry over the past few years, largely as a result of shale drilling, has turned the United States from a major energy importer into a petroleum powerhouse. That has led Saudi Arabia and Russia, the world's two other leading oil producers, but which have not always seen eye to eye, to create a bloc large enough to influence prices.

But the pre-meeting fireworks with Iran showed how hard it would be to preserve unity among other producers, now that prices have risen. Tehran, in particular, has been infuriated by the Saudi call for increased production. The country has also been particularly affected by the rise in United States oil exports -- the resurgent American sector has made it easier for Mr. Trump to risk reimposing sanctions on Iran, which throttle back what had been rising oil exports from the Gulf country.

Venezuela is also vulnerable to American pressure, thanks to the strengthened United States energy industry. Sanctions from the United States have prohibited the sale and purchase of Venezuelan debt, including bonds issued by the state oil company, Petróleos de Venezuela, and banning the use of the country's digital currency, the petro.

That has crimped the energy company's ability to refinance $50 billion in bonds that it has defaulted on since last year. Elsewhere, fighting in Libya has cut into global supplies, as well.

''Stability is elusive,'' Edward L. Morse, the head of commodities research at Citigroup, said at a seminar in Vienna.

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Saudi Arabia's energy minister, Khalid al-Falih, has led a shift among major producers to increase the production of crude oil. (PHOTOGRAPH BY HEINZ-PETER BADER/REUTERS)

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THE WALL STREET JOURNAL.
U.S. EDITION

EXCHANGE --- Heard on the Street: Oil Deal Is Nothing to Gush About --- OPEC's agreement helped oil prices rise for the day -- though a lot more crude is headed to market

By Spencer Jakab
544 words
23 June 2018
The Wall Street Journal
J
B14
English

[Financial Analysis and Commentary]

OPEC is "at it again," to borrow Donald Trump's wording, but not in the way he imagined.

The oil cartel reached a preliminary decision Friday to boost output by an effective 600,000 barrels a day, six months before its agreement was set to expire. The Organization of the Petroleum Exporting Countries displayed a show of unity that seemed unlikely earlier in the week, complicated, ironically enough, by the president's tweet. Major producer Iran cast doubt on OPEC reaching an agreement as recently as Thursday, sniping that the group "is not part of the Department of Energy of the United States."

The fact that the cartel came together in the end helped **oil prices** rise on Friday, though the output boost is only **bullish** compared with some of the larger numbers that were being tossed around a day or two ago. Compared with expectations of a 300,000- to 600,000-barrel-a-day increase coming out of a meeting between Saudi Crown Prince Mohammed bin Salman and Russian President Vladimir Putin at the opening game of the World Cup a week ago, it is **bearish**. Some convoluted oil math explains why.

OPEC's official output increase may be 1 million barrels a day, but the effective number from the cartel will be roughly 600,000 barrels a day because some members can't meet higher quotas. But Russia will boost production too, as will some non-signatories, resulting in roughly 1 million extra barrels a day, which should pressure **oil prices** as the year goes on.

This is why the math of the oil market is important. The current "OPEC plus" agreement, implemented in January 2017, was extraordinarily successful at raising prices and slashing inventories. The exporters jointly agreed to cut output by 2.2 million barrels a day. Of that amount, OPEC's portion was about 1.6 million barrels a day, but the signatories actually reduced output by about 2.15 million barrels a day if one compares last month's production with the October 2016 reference month. All the difference, and then some, can be explained by Venezuela's meltdown -- an 850,000-barrel a day drop and growing. Another 500,000-barrel-a-day-or-so drop not counted in that total came from politically fragile Nigeria and Libya, whose production isn't counted in the deal numbers.

When all is said and done, OPEC may effectively boost output by something like 700,000 barrels a day by the end of 2018, according to analysts at Barclays who assume that Libya will be able to raise output. Throw in Russia's coming boost and the total output boost may be right around 1 million barrels a day. That is slightly less than what had been expected in recent days.

After its most successful action in decades, OPEC has managed to maintain harmony. For a day, at least, that overshadows the news that a lot more crude is headed to market.

page,5043

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Business Day

OPEC , After Bolstering Prices, Considers Ramping Up Oil Production

By Stanley Reed
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22 June 2018
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English

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But the pre-meeting fireworks with Iran showed how hard it would be to preserve unity among other producers, now that prices have risen. Tehran, in particular, has been infuriated by the Saudi call for increased production. The country has also been particularly affected by the rise in United States oil exports — the resurgent American sector has made it easier for Mr. Trump to risk reimposing sanctions on Iran, which throttle back what had been rising oil exports from the Gulf country.

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Follow Stanley Reed on Twitter : @stanleyreed12. Clifford Krauss contributed reporting from Houston.

* U.S. **Oil Prices** Hit $70 a Barrel for First Time Since ’14

* Trump Criticizes OPEC, Calling **Oil Prices** ‘Artificially’ High

* Lower **Oil Prices** Force Saudis to Widen Their Circle of Friends

Saudi Arabia’s energy minister, Khalid al-Falih, has led a shift among producers to raise production of crude oil. | Heinz-Peter Bader/Reuters

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THE WALL STREET JOURNAL.

Heard on the Street
Markets

What Is Ailing the Drug Industry? 'Big pharmaceuticals' shares are underperforming; 'victims of their own success'

By Charley Grant
764 words
22 June 2018
06:00 AM
The Wall Street Journal Online
WSJO
English

It's a golden age for drug development, but the major pharmaceutical companies aren't enjoying the good times.

U.S. health-care spending regularly grows faster than inflation and has reached about 18% of gross domestic product. Prescription drugs are a major component of that sum. The Centers for Medicare and Medicaid Services projects that total U.S. drug spending will rise by 68% to $600 billion by 2026. Meanwhile, the Food and Drug Administration is approving new medicines at a brisk rate and venture capitalists have poured billions into biotech startups.

Yet the **stock market** is treating drugmakers as a struggling industry. The NYSE Arca Pharmaceutical Index has underperformed the **S&P 500** by nearly 30 percentage points over the past two years. Not all drug companies are suffering. Over that same time frame, an index of small biotech stocks has beaten the **S&P 500** by more than 50 percentage points.

One reason for the big stocks' underperformance: "Many larger pharma and biotech companies alike have now become victims of their own success," says Jared Holz, a health care sector specialist at Jefferies. More money is chasing fewer opportunities, lowering returns and forcing companies that want to grow to take multibillion-dollar risks.

For instance, recent years have produced a trove of innovative medicines. The success stories include drugs that cure hepatitis C within months for most patients. New ways to fight cancer have shown spectacular results in certain patients and generated billions of dollars in revenue for drug companies. Other novel technologies like gene therapy have the potential to help previously untreatable patients.

But the march of scientific progress has translated into fewer unmet medical needs for the industry to tackle. Statins, the cholesterol drugs patients take daily for years that were the industry's best selling drug class in decades past, are now available as cheap generics. Today, even great discoveries treat much less common diseases with smaller pools of patients. To make sense commercially, such drugs often carry shockingly high prices per dose, inviting a political backlash.

Drugmakers are more dependent on their big hits than ever. Twenty years ago, Bristol-Myers Squibb's best selling statin, Pravachol, generated annual sales of $1.6 billion. This year, analysts expect four drugs from Bristol-Myers will top $2 billion in sales. Yet the company's total sales has increased by a fairly tame 18% in that time frame.

That can pose a challenge since today's blockbuster drug is a future revenue hole that needs to be filled when competition emerges. Developing drugs has never been easy, but that chase has become much more expensive.

New drug candidates are increasingly complex biologic drugs, not traditional molecules. A member survey conducted by the Pharmaceutical Research and Manufacturers of America found that total spending on research and development topped 20% of sales in 2016, the highest on record. In 1980, that spending accounted for less than 9% of sales.

Companies that can't develop enough successful new candidates internally need to buy them. About 50% of drugs in the industry's pipeline come from external sources, a 2016 research paper found.

That need to find new drugs, coupled with low interest rates, has increased the temptation to make splashy acquisitions. There have been more than $190 billion worth of global biotech and pharma acquisitions announced so far this year, according to Dealogic, on pace to top the record of $315 billion set in 2015.

Deal prices are ratcheting higher, too. The average transaction value this year tops $335 million. In 2011, that figure was about $68 million, meaning companies are paying more for unproven drugs.

The strategy can be successful: Gilead Sciences completed one of the greatest deals in the industry's history in 2011 when it bought Pharmasset for $11 billion, getting what became its $56 billion hepatitis C drug. But other deals of similar size have fared much worse. Alexion Pharmaceuticals bought Synageva BioPharma for $8.4 billion, but the deal didn't result in meaningful growth. Celgene spent more than $7 billion to acquire Receptos in 2015. But the acquired drug hasn't won FDA approval, and Celgene stock has shed more than 40% of its value since last fall.

Trying to find drugs that can meaningfully boost growth has become a high-stakes game of chance. Lately, the industry and investors have been on a losing streak.

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WSJ PRO FINANCIAL REGULATION

Markets

SEC Probes Whether Companies Rounded Up Earnings Per Share; Regulators investigating the case of the missing '4'

By Dave Michaels
882 words
22 June 2018
04:58 PM
WSJ Pro Financial Regulation
RSTPROFR
English

WASHINGTON—Federal regulators are investigating the case of the missing "4," exploring the numeral's conspicuous absence in quarterly reports that could mean companies have improperly rounded up their earnings per share to the next highest cent, according to people familiar with the matter.

Enforcement officials at the Securities and Exchange Commission have sent queries to at least 10 companies, asking the firms to provide information about accounting adjustments that could push their reported earnings per share higher, one person familiar with the matter said.

The queries follow the release of an academic paper that found evidence of companies nudging up earnings results. The academic research found the number "4" appeared at an abnormally low rate in the tenths place of companies' earnings per share. Reporting that figure as "5" or higher allows a firm to round up its earnings per share another cent.

For instance, a company with earnings of 55.4 cents a share would round to 55 cents a share, while a company with earnings of 55.5 cents a share would round to 56 cents.

Public companies have strong incentives to report higher earnings per share, particularly those followed by Wall Street analysts whose quarterly forecasts are used to benchmark corporate performance. Investors often snap up shares of companies that beat expectations, even by a cent, and, likewise, sell shares of companies that miss their forecasts.

The names of the companies that received the SEC's queries couldn't be learned. The SEC didn't immediately respond to a request for comment.

The investigation is in its early stages, one of the people said. Accounting rules offer some discretion for when managers recognize revenue or expenses, so quarterly adjustments can be legal even when they boost reported earnings per share.

The researchers, Nadya Malenko and Joseph Grundfest, referred to the dynamic they detected as "quadrophobia." The paper was widely read within the SEC, one of the people said.

The SEC has for several years sought to bring more cases over accounting fraud. Probes involving financial reporting previously had taken a back seat to investigations over complex financial instruments and insider trading after the 2008 financial crisis.

In 2012, the SEC announced it had developed an "accounting quality model" that could scan companies' financial statements for anomalies that might indicate fraud.

SEC economists replicated aspects of Dr. Malenko's and Mr. Grundfest's study and found similar results—cases where the digit "4" rarely appeared over a large number of accounting quarters, one person said.

Dr. Malenko's and Mr. Grundfest's paper, which hasn't appeared in an academic journal and was last updated in 2014, showed that companies with signs of strategic rounding over many quarters were more likely to be charged with accounting violations, restate earnings, or become targets of shareholder lawsuits.

"The rounding itself might not be fraud, but it signals a certain aggressive approach to accounting practices," said Dr. Malenko, a finance professor at Boston College. "It can predict more serious accounting violations."

The research rests on an assumption that every number should appear in the tenths place 10% of the time. After reviewing nearly 951,612 quarterly results for over 25,000 companies from 1980 to 2013, however, the authors found that "4" appeared in the tenths place only 8.6% of the time. Both "2" and "3" were also underrepresented in the tenths place; all other digits appeared more frequently than would be expected by chance.

The researchers checked their assumption by examining other metrics that tend to be less correlated with **stock price** moves than EPS. For those ratios, including sales per share and operating income per share, the digit "4" appeared in the tenths place about 10% of the time in all years of the researchers' sample data.

Companies closely followed by analysts were more likely to report fewer "4s," as were both the largest and the smallest firms. Firms with high **stock market** valuations, as well as those with lower earnings per share, were also more likely to show signs of rounding up their earnings, the authors found.

As The Wall Street Journal reported in 2010, computer maker Dell Inc. didn't report earnings per share with a "4" in the tenths place between its 1988 initial public offering and 2006. The likelihood of that happening by random chance was 1 in 2,500.

In July 2010, Dell paid $100 million to settle SEC charges that it misled investors about the source of earnings and used "cookie jar" reserves to manipulate quarterly results. Reversing excess reserves turned them into income, which allowed Dell to meet quarterly EPS targets in some cases, the SEC said.

At the time, a Dell spokesman said the company's financial-reporting practices are "rigorous" and the company is "committed to ongoing transparent and accurate reporting."

Pushing up EPS by a 10th of a cent doesn't require a significant accounting adjustment, making it easier for companies to nudge the ratio higher without attracting much scrutiny. In 2013, the mean additional amount of earnings required to do so was $222,000, the researchers found.

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WSJ PRO PRIVATE EQUITY

Markets
Activist Ends Campaign Against Oil Company, Walks Off with $90 Million; Kimmeridge sold its stake after trying to persuade Carrizo to change its drilling strategy or merge with a rival

By Ryan Dezember
558 words
22 June 2018
11:05 AM
WSJ Pro Private Equity
RSTPROPE
English

Kimmeridge Energy Management Co. folded its activist campaign against Carrizo Oil & Gas, but it is retreating with about $90 million profit.

The New York investment firm this week sold its stake in the Houston energy producer following a sharp rise in its shares since spring. Kimmeridge netted a nearly $90 million profit on its roughly $100 million investment in Carrizo shares, according to people familiar with the matter.

Kimmeridge had urged Carrizo to sell its South Texas drilling fields and focus instead on those in West Texas, or combine with a rival. But the investment firm sold out of all but a sliver of its 8.1% stake in Carrizo this week after the company's chief executive went on a television program popular with investors to tout Carrizo's strategy of drilling in both West and South Texas, said Ben Dell, the firm's founder and managing partner.

Kimmeridge disclosed the sale in a securities filing Friday. Carrizo didn't respond to requests for comment.

Carrizo's shares have risen 81% since early April when Kimmeridge disclosed that it had raised its stake from 4.9% and planned to urge the company to focus on the Permian Basin and perhaps find a merger partner. Carrizo's shares shot up 11% the day of the disclosure and rising commodity prices have helped push the stock higher, to a point. The SPDR S&P Oil & Gas Exploration & Production exchange-traded fund gained 19% in that time.

The sharp rise in Carrizo's stock has occurred as **oil prices** have plunged in the Permian, the result of the region's prolific wells overwhelming pipelines that connect the Texas deserts to markets along the Gulf Coast. At the same time, crude prices in the Eagle Ford shale in South Texas have been above the main U.S. benchmark due to those wells' proximity to shipping terminals near Houston, where crude can fetch higher international **oil prices**.

Carrizo CEO Chip Johnson appeared on CNBC's "Mad Money" with host Jim Cramer on Tuesday to tout the benefits of its dual-drilling-basin strategy. Mr. Johnson said on the show that although Permian barrels were selling for around $12 below the main U.S. benchmark, West Texas Intermediate, those produced in the Eagle Ford are selling for about $8 above the oft-cited **oil price**.

"We're shifting rigs and (hydraulic-fracturing) crews there as fast as we can," Mr. Johnson said on the program.

Mr. Cramer called the move "the pivot of the year."

Kimmeridge had been urging Carrizo's management to sell its Eagle Ford acreage while the price was high and use the proceeds to bulk up in the Permian ahead of pipeline construction that is expected to clear the bottleneck, Mr. Dell said. But the private-equity executive said he took from the program that Mr. Johnson would be unwilling to do so and had "painted himself into a corner" with his remarks.

"We saw that interview and thought, ‘we aren't on the same page,'" he said. "It's the ultimate in short-termism."

Write to Ryan Dezember at ryan.dezember@wsj.com

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THE WALL STREET JOURNAL.

Markets

Why Gold's Tumble Signals Confidence in U.S. Economy; There are even some gold bulls wondering if the precious metal's yearslong rebound is ending

By Amrith Ramkumar
738 words
22 June 2018
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The Wall Street Journal Online
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English

Gold slumped nearly 3% in the past week, hitting its lowest levels of the year—the latest sign that investors are betting on continued U.S. growth and shrugging off trade tensions between the world's two largest economies.

Gold's prolonged retreat comes after months of rangebound trading that followed three straight quarterly gains. The recent slump is causing some **bullish** investors to wonder whether the haven metal's yearslong rebound might be coming to an end.

While gold stayed above $1,300 a troy ounce for much of the year, investors are watching to see if further **volatility** pushes prices below Thursday's close of $1,267.20.

With prices still well below 2011 records, some

had anticipated that investor fears would push gold higher as investors flocked to safer assets. Instead, the metal has languished as economic-growth momentum has shifted to the U.S. and the Federal Reserve has continued to raise interest rates. The metal's weakness has coincided with the dollar reaching a near one-year high and the yield on the 2-year Treasury piercing 2.5% for the first time since 2008.

The developments are causing some analysts to predict bullion will extend its decline, with few signs that a recession will derail the nine-year old **bull market** in stocks and push investors back to the precious metal.

"Gold doesn't seem to be the vogue play right now," said Nathan Thooft, senior managing director of global asset allocation at Manulife Asset Management. "People would rather own short-term Treasurys or make a dollar bet than make a gold bet."

In addition to making gold less attractive to some, a stronger dollar makes gold more expensive for overseas buyers.

That is another reason the metal had its worst five-day stretch in almost a year through Thursday even as President Donald Trumpescalated a trade conflict with China, asking his administration to identify a new list of $200 billion in Chinese goods that would be penalized with tariffs.

Despite occasional fears over trade, global investors have been assured by growth in the U.S. that is on track to exceed a 4% pace in the three months ending in June, which would be the fastest of any quarter in almost four years. That has given the Fed a free hand to raise interest rates twice already this year and target two more increases for 2018, a more aggressive pace than the central bank had previously projected.

Growth has slowed in other parts of the world, but the World Bank estimates the global economy will still grow 3.1% for the second straight year, letting other major central banks also tighten monetary policy.

"As long as the market feels that the world economy is going to be able to sustain higher rates, the price of gold is going to be trading in a range," said Chris Mancini, an analyst at Gabelli Gold Fund. "It's very frustrating."

Shares of gold miners have also lost their luster. The NYSE Arca Gold Miners Index has fallen in four of the five sessions through Thursday, bringing its year-to-date losses to 6.4%.

Speculative investors are turning cautious. Hedge funds and other speculative investors have lowered net bets on higher prices by more than 40% in 2018, pushing them in late May to their lowest levels since last summer, Commodity Futures Trading Commission data show. Flows into gold-backed exchange funds have remained tepid and demand for American Eagle gold coins, a proxy for physical demand, recently hit a multiyear low.

Some say that rising inflation could lead some investors to turn to gold as a hedge.

But adding to worries for bulls, gold has been moving more in lockstep with other materials such as oil and copper, stoking fears that if investors sell commodities, the yellow metal will also suffer. U.S. crude futures are more than 6% below their May multiyear highs, and copper dropped in seven of the last nine sessions entering Friday.

"What broke the back for gold was really the commodity selloff," according to Vinay Pande, head of short-term investment opportunities at UBS Global Wealth Management.

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

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THE WALL STREET JOURNAL.

U.S. Markets
Markets
Dow Suffers Biggest One-Week Loss Since March; Trade tensions spook investors

By Riva Gold and Akane Otani
638 words
22 June 2018
05:07 PM
The Wall Street Journal Online
WSJO
English

* Crude oil rises after OPEC deal

* Dow rises after eight straight losses

* Biggest weekly outflows from EM equities since 2016

The **Dow Jones Industrial Average** rose Friday but posted its biggest one-week slide since March as escalating tariff tensions drove investors out of companies they fear could suffer under tighter trade conditions.

Stocks wobbled throughout the week, with shares of industrial firms, agricultural companies and auto makers sliding as investors feared global trading relations were becoming increasingly fractured.

President Donald Trump asked his administration Monday to identify an additional $200 billion of Chinese goods that would be penalized with tariffs. He then threatened Friday to impose a 20% tariff on European cars after the European Union began imposing duties on U.S. products ranging from bourbon whiskey to Harley-Davidson motorcycles.

The moves contributed to unease among investors, who worry that such fractious approaches could hinder global growth at a time when many already believe that economic momentum is fading.

The Dow industrials fell eight straight sessions through Thursday—notching its longest streak of declines in more than a year. As investors broadly shed risk, investors withdrew the biggest weekly amount from emerging-market equities, financials and investment-grade bond funds since 2016, according to Bank of America Merrill Lynch.

"We're starting to see some corporate impact to some of the rhetoric coming out of Washington," said Barbara Reinhard, head of asset allocation at Voya Investment Management. "Potentially targeting the auto sector has a far greater economic impact than anything that has been done so far."

The Dow industrials rose 119.19 points, or 0.5%, to 24580.89 Friday but slid 509.59 points, or 2%, for the week.

The **S&P 500** added 5.12 points, or 0.2% to 2754.88 and fell 24.78 points, or 0.9% for the week, while the **Nasdaq Composite** edged down 20.13 points, or 0.3%, to 7692.82 and lost 53.56 points, or 0.7%, for the week.

Stocks got a boost Friday from energy shares, although they weren't enough to offset broad declines throughout the week from other sectors.

Dow component Chevron rose $2.51, or 2%, to $125.10 and Exxon Mobil added $1.69, or 2.1%, to $81.38 after members of the Organization of the Petroleum Exporting Countriesagreed to a deal to join other big producers in boosting oil production by about 600,000 barrels a day.

The move came as a relief to investors who had been expecting the cartel to decide to boost output even further, sending U.S. crude for August delivery up 4.6% to $68.58 a barrel—its biggest one-day percentage gain since 2016.

Industrial shares in the **S&P 500** rose Friday but posted weekly declines, with Caterpillar down $10.08, or 6.7%, to $139.94 for the week and Boeing losing $18.97, or 5.3%, to $338.91 over five sessions.

Elsewhere, the Stoxx Europe 600 rose 1.1% but fell 1.1% for the week, weighed down by shares of European auto makers.

Japan's Nikkei Stock Average fell 0.8% Friday and 1.5% for the week, while the Shanghai Composite Index dropped 4.4%, its worst week since February.

Write to Riva Gold at riva.gold@wsj.com and Akane Otani at akane.otani@wsj.com

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THE WALL STREET JOURNAL.

Markets

The Score: The Business Week in 7 Stocks; The Journal's weekly guide to the ups and downs of the business world

By Laine Higgins and Caitlin Ostroff
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22 June 2018
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Boeing Co. - ▼ 3.8% Tuesday

Investors are waking up to the idea that the trade war between the U.S. and China could be the real deal. After China pushed back against U.S. tariffs on $50 billion in Chinese products, saying it would levy similar penalties against American goods, President Donald Trump threatened Monday to retaliate with another $200 billion in tariffs. That sent a wide swath of the **stock market** tumbling Tuesday. Boeing, which counts China as its largest market, single-handedly took 94 points off the **Dow Jones Industrial Average** that day.

Amazon.com Inc. - ▲0.9% Wednesday

The health-care partnership jointly announced by Amazon, Berkshire Hathaway Inc. and JPMorgan Chase & Co. in January now has a face. The business giants on Wednesday appointed Dr. Atul Gawande as chief executive of a yet-to-be-named company tasked with tackling rising employee health-care costs. Dr. Gawande's resume includes practicing surgery at Brigham and Women's Hospital, teaching at Harvard, writing for the New Yorker and serving as executive director of Ariadne Labs, commitments he will maintain in various capacities when he begins his new role July 9.

Walgreens Boots Alliance Inc. - ▲5.3% Wednesday

For the first time since 1907, General Electric Co. will not trade as part of the 30-stock **Dow Jones Industrial Average**. It's ceding its spot to drugstore retailer Walgreens, a move that gives more weight to the consumer and health-care sectors of the U.S. economy. Walgreens, which dates back to 1901, has expanded in recent years by merging with a European drug wholesaler and buying up stores from Rite Aid Corp. Its shares have declined 13% in the past year, and it now has a market capitalization of $67 billion. GE has declined 53% in that same span.

Starbucks Corp. - ▼9.1% Wednesday

Starbucks' stock was in need of a pick-me-up Wednesday after the company announced it would close 150 U.S. stores and expected global same-store sales growth of 1% in the current quarter, far below Wall Street's expectations. The closures, which are concentrated in urban areas where stores are clustered and rents are high, are a sign the coffee giant overestimated Americans' caffeine cravings and expanded too quickly. Chief Executive Kevin Johnson said the company now plans to focus on growing the chain's "digital relationship" with customers.

21st Century Fox - ▲7.5% Wednesday

Walt Disney Co. upped the ante in its bidding war with Comcast Corp. for 21st Century Fox assets Wednesday, raising its offer to more than $70 billion in cash and stock. That's up from its original $52.4 billion stock bid and tops Comcast's unsolicited $65 billion all-cash proposal. The Fox board accepted the offer, which equates to $38 a share, describing it as "superior to the proposal" made by Comcast earlier this month. If the deal closes, Fox shareholders would own 19% of the combined company. (21st Century Fox and Wall Street Journal-parent News Corp share common ownership.)

Intel Corp. - ▼2.4% Thursday

Intel Chief Executive Brian Krzanich resigned Wednesday after the company learned that he'd had a relationship with an employee, a violation of company policy. Chief Financial Officer Robert Swan will serve as interim CEO until the company's search yields a replacement leader. If the board picks an outsider, it will be the first in the chipmaker's 50-year history. To counter the news, Intel offered a rosy second-quarter forecast ahead of its earnings call on July 26, but investors uncertain about the executive shake-up sent the stock down anyway.

Chevron Corp. - ▲2% Friday

Members of the Organization of the Petroleum Exporting Countries agreed Friday to boost output by about 600,000 barrels a day. That was less than some observers had expected, and the news that the world wasn't suddenly going to be awash in oil sent crude prices higher. The energy sector led the **S&P 500**, while Chevron and Exxon Mobil Corp. collectively added 29 points to the Dow's rise. The deal still needs final approval from Russia and other non-OPEC members. That's expected to come Saturday.

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THE WALL STREET JOURNAL.

Markets
U.S., Russian Top Energy Officials to Meet Next Week; Rick Perry will host Alexander Novak; meeting comes as Trump pushes oil producers to pump more

By Timothy Puko and Benoit Faucon
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22 June 2018
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English

Energy Secretary Rick Perry will host Russia's energy minister for a meeting in Washington next week, according to people familiar with the planning, putting the top energy officials from the world's largest oil and gas producers in the same room at a time when relations between the countries are increasingly under the spotlight.

It is the latest outreach from President Donald Trump's administration as it continues a push for better relations with Russia. White House national security adviser John Bolton will also travel to Russia this month to discuss a possible summit meeting between Mr. Trump and Russian President Vladimir Putin. Russian Oil Minister Alexander Novak is to meet Mr. Perry at Energy Department headquarters on Tuesday, according to the people.

The meeting is supposed to focus on better cooperation in energy between the two countries, according to a Russian official. The countries have become direct rivals in global markets in recent years as the shale-drilling boom pushed the U.S. past Russia as the world's largest oil and gas producer. Mr. Trump has threatened to use that new prowess as a political bulwark against Russia. Political sanctions still target the Russian energy industry, and Russian-backed propaganda has targeted the U.S. industry.

The meeting would come, though, as the countries' interests have begun to align. Gasoline prices have started to rise just ahead of midterm elections in the U.S., and Mr. Trump and his team have responded by trying to prod the world's other big oil producers to pump more. Russia also wants to increase output and lower prices to about $60 a barrel, and is using its increasing sway in global politics to do it.

Russia and Saudi Arabia established an alliance in 2016 that has become maybe the largest single variable for **oil prices**. They first agreed to cut output, a move largely responsible for the recent rise in **oil prices** to 3 1/2-year highs. And Russian lobbying with Iran also helped the Organization of the Petroleum Exporting Countries to secure an output boost of 600,000 barrels a day, which the group announced Friday.

Russia's willingness to take positions similar to those of the Trump administration has puzzled many in OPEC. An OPEC official compared Russia's stance to a game of "Russian roulette," while another OPEC official said that in the oil world, "geopolitics have never been more confusing."

The meeting between Messrs. Perry and Novak will come three days after the end of OPEC-led meetings in Vienna and on the first day of the World Gas Conference taking place in Washington. The U.S. is also an increasing exporter of natural gas, competing with Russia in a global market where both have tried to use their exports as a way to influence or help political allies.

Mr. Trump has been pressing Germany to drop its support for a major gas pipeline project coming from Russia as the price for avoiding a trans-Atlantic trade war, according to German, U.S. and European officials. And Mr. Perry also plans a joint meeting during next week's gas conference with several European leaders to promote the Three Seas Initiative, largely designed to blunt Russia's influence with better energy ties between European nations.

Messrs. Perry and Novak have met before, speaking on a panel together at the World Economic Forum in Davos, Switzerland. And while energy meetings like these were frequent while Barack Obama was president, the world has changed dramatically since then, said Jonathan Elkind, the Energy Department's assistant secretary for international affairs at the end of the Obama administration.

"This is all exceedingly complicated and needs to be worked through in a way that is serious-minded and sober and careful, but that advances U.S. interests," said Mr. Elkind, now at Columbia University's Center on Global Energy Policy. "The world is a better place if we are having serious and direct conversations with the Russians about the areas where we disagree."

Despite these conflicts, Mr. Trump at many times has praised Russia and Mr. Putin. And he has called for closer relations with the country despite its incursion into Crimea in 2014 and concerns about its interference in foreign elections.

Special counsel Robert Mueller is investigating Russian efforts to influence the 2016 presidential election and Trump associates' ties to that effort. That probe has produced 20 public indictments or guilty pleas; Mr. Trump has denied having worked with Russia during the campaign.

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U.S. EDITION

Big Oil Pulls Back, Threatens Supplies

By Sarah Kent
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22 June 2018
The Wall Street Journal
J
B1
English

LONDON -- For the past two years, big oil-exporting nations reined in production to boost prices.

But rather than responding with fresh investment, Western oil companies have retrenched, a move many now say threatens a longer-term supply crunch.

As oil executives descend on Vienna this week, members of the Organization of the Petroleum Exporting Countries, Russia and other big producers are looking to broker a deal to pump more crude now that prices have climbed.

A decision to move forward with the plan to lift output could have a big effect on short-term **oil prices** and prices at the gasoline pump.

But further out, industry spending on new oil fields will have a more lasting impact on both supply and prices.

Since **oil prices** plunged in 2014, the world's biggest publicly listed Western oil companies have slashed their capital spending by roughly 40%, according to data from investment bank Jefferies. While Brent crude prices have climbed 9.2% this year, flirting with their highest level since 2014 last month, executives at big oil companies have largely vowed to keep a tight lid on spending.

"We're going to maintain the capital discipline," BP PLC Chief Executive Bob Dudley said this month.

The companies, including Chevron Corp. and Royal Dutch Shell PLC, are moving cautiously under pressure from investors, who were burned by big budgets and poor returns when prices were high. Instead of spending on new projects, these companies are paying down debt and generating cash for those skeptical investors, with buybacks or higher dividends.

But without fresh spending on new oil production, the world could slip into a supply crunch after 2020, the International Energy Agency has warned. The sector needs to raise its spending by a third just to maintain production at current levels in coming years, according to Wood Mackenzie, an oil-focused consulting firm.

"The industry isn't spending enough to sustain itself," said Angus Rodger, a Wood Mackenzie research director.

There are short-term risks, too, executives and analysts say. Forecasts for oil demand are rising.

Today's cushion of oil stored in inventories, which protects consumers from price shocks, is the lowest in years. Fields that showed early promise can deplete faster than expected. Geopolitical events in Venezuela, Iran and Libya have also cut into supply.

"If we get a surprise in terms of decline rates or demand, there's a chance we'll see a significantly tighter market," said Eirik Waerness, chief economist at Norwegian energy company Equinor ASA, formerly called Statoil. "The price reaction could be very strong."

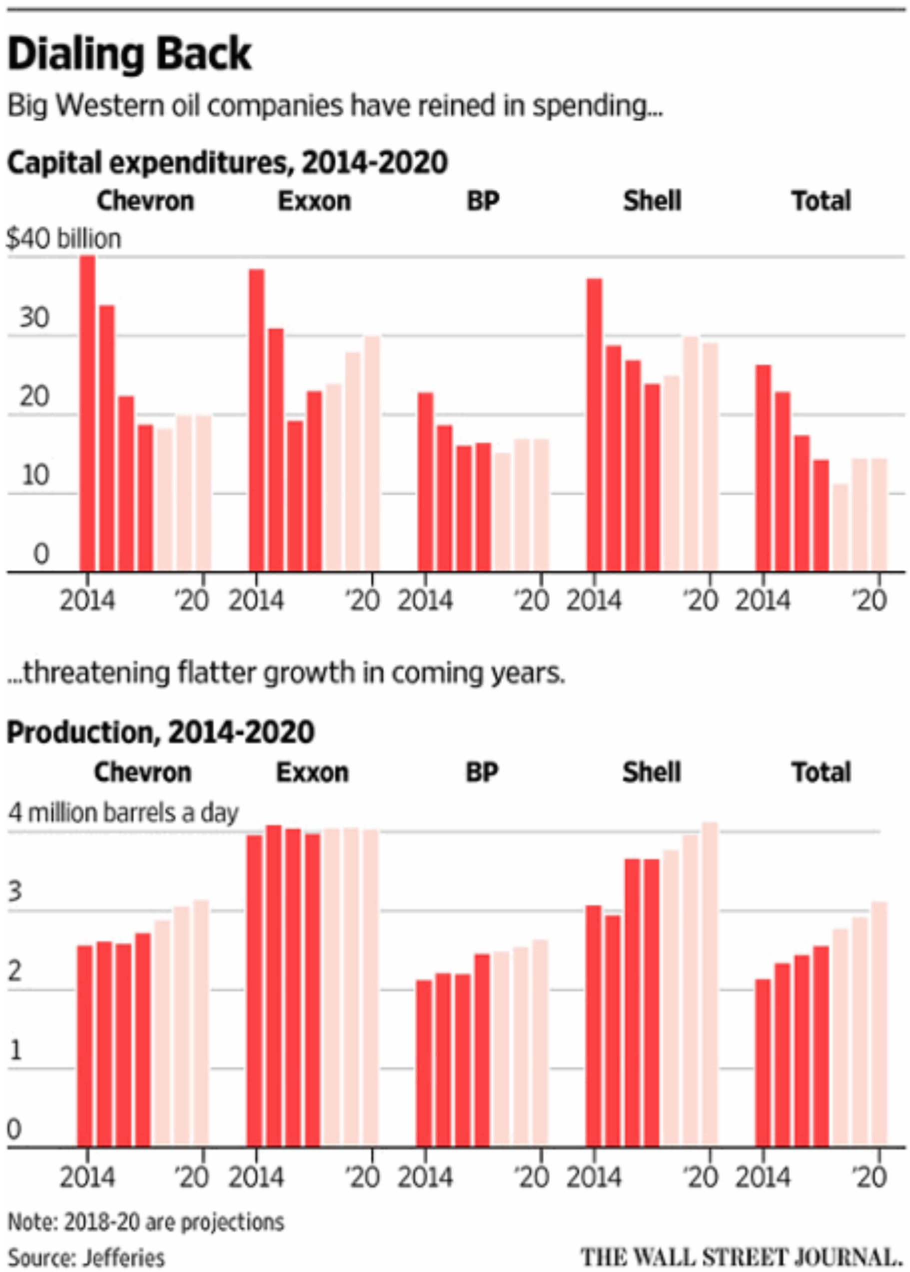
Despite the spending cuts, production continues to increase among big companies in part due to investment from years past.

Jefferies estimates the world's biggest publicly listed Western oil companies will increase output roughly 10% by the end of the decade, compared with last year.

And while budgets remain capped, companies are beginning to approve new projects again, taking advantage of substantial success in lowering costs. Nonpublic companies, including the state-owned firms that pump OPEC crude, have also promised they will continue to pour money into developing fields.

Last year, 32 major new developments got the go-ahead, and 16 have been approved this year, according to Wood Mackenzie. Many of those new projects, though, are natural gas, rather than oil. Companies are also shifting their spending focus from long-term projects to shorter-cycle shale developments that deliver faster returns.

"We have a possible future of crisis," OPEC Secretary-General Mohammad Barkindo warned at an industry conference in March. "The global industry needs to focus on the threat of underinvestment."



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THE WALL STREET JOURNAL.

Markets

Copper Closes Slightly Higher as Trade Anxiety Continues; Prices have fallen 7.9% in June, with some analysts worried protectionist trade policies will weaken commodity demand

By David Hodari and Amrith Ramkumar
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English

Copper prices swung between small gains and losses before closing slightly higher Friday, with global investors still anxious about recent trade barbs between the U.S. and China.

Front-month copper for June delivery closed up 0.2% at $3.0325 a pound on the Comex division of the New York Mercantile Exchange but still capped off its worst two-week stretch in two years. Prices have fallen 7.9% from their year-to-date highs hit earlier this month, with some analysts worried that protectionist trade policies will slow global growth and weaken commodity demand.

Early this week, President Donald Trumpescalated a trade conflict with China, asking his administration to identify a new list of $200 billion in Chinese goods that would be penalized with tariffs. China is the world's largest commodity consumer, accounting for about 50% of copper demand, and some analysts are increasingly worried a growth slowdown there could hurt industrial metals.

Copper's whipsaw **volatility** during June suggests that "the market is not as robust as previously thought," said Carsten Menke, commodity analyst at Julius Baer.

"There was a lot of length in the market probably based on a still-positive macroeconomic outlook, but investors have been getting cold feet as trade tensions have heated up," Mr. Menke said.

Analysts are monitoring conflicts between large miners and emerging-market countries and wage negotiations for signs of supply disruptions that could boost the red metal, with steady supply figures also dragging on copper throughout the year.

Among precious metals, front-month gold for June delivery was also little changed and closed up less than 0.1% at $1,267.40 a troy ounce. Prices have fallen to their lowest level since December on worries about higher interest rates and with the dollar hitting its highest level in nearly a year earlier this week. Gold struggles to compete with yield-bearing assets such as Treasurys when rates rise, and a stronger dollar makes the metal more expensive for overseas buyers.

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Streetwise: How to Invest in a Trade Spat

By James Mackintosh
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22 June 2018
The Wall Street Journal
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B1
English

Markets follow a well-worn pattern after Donald Trump's pronouncements, a pattern that followed those on taxes, North Korea and trade. There is a sharp reaction -- up or down -- on the first news, fading as doubts that the president is willing to follow through set in. Then there is another panic on the realization that he is serious, and finally the market prices in the details of whatever compromise he settles on.

The Trump trade war briefly reached the realization phase on Tuesday, but markets are still waking up to the idea that trade battles are more than a sideshow. Investors who think China won't back down still have plenty of opportunity to get out. They also have a problem: get out of what, exactly?

It is exceptionally hard to work out how to price in a prolonged trade fight. So far, investors have turned to simple rules of thumb, but ignoring the complexities won't make them go away. The basic rule is to avoid companies with big Chinese exposure, particularly those that could also make handy high-profile targets for foreign retaliation.

So far, that has meant selling shares in Caterpillar and Boeing, preferring smaller stocks to bigger ones, and preferring the U.S. to emerging markets, especially China and big trading partners such as South Korea.

"There were a lot of assumptions that these tariffs were simply negotiating tactics and we would come up with some sort of agreement and they wouldn't be put in place," said Robert Baur, chief global economist at Principal Global Investors in Des Moines, Iowa. "That's clearly not right, but how far it is going to go, we don't know."

The first corporate information knocked shares in German car maker Daimler down 4% on Thursday. It said profit would be hurt as China's retaliatory tariffs on U.S. light trucks hit Mercedes SUV exports from its Alabama factory. But information about other companies is sparse, partly because supply chains are so complex.

Tuesday's price drops showed that China-related stocks in the U.S. are sensitive to trade fears. All but one of the 14 **S&P 500** members that make more than a quarter of their revenue from China declined by more than the index.

Yet, the same stocks suggest that trade-war fears haven't sunk in properly, with six of them up and seven down since the day before the announcement of tariffs on the first $50 billion of Chinese goods in March. Caterpillar and Boeing tell the same story, with their shares falling hard this month but being dominated by other issues until then.

This makes sense. It is hard to price in something you don't understand, and the implications of a trade battle are obscure, at best. Not only do we not know precisely which products will be targeted in the next round, or how long the tariffs will last, but we have little understanding of complex corporate supply chains.

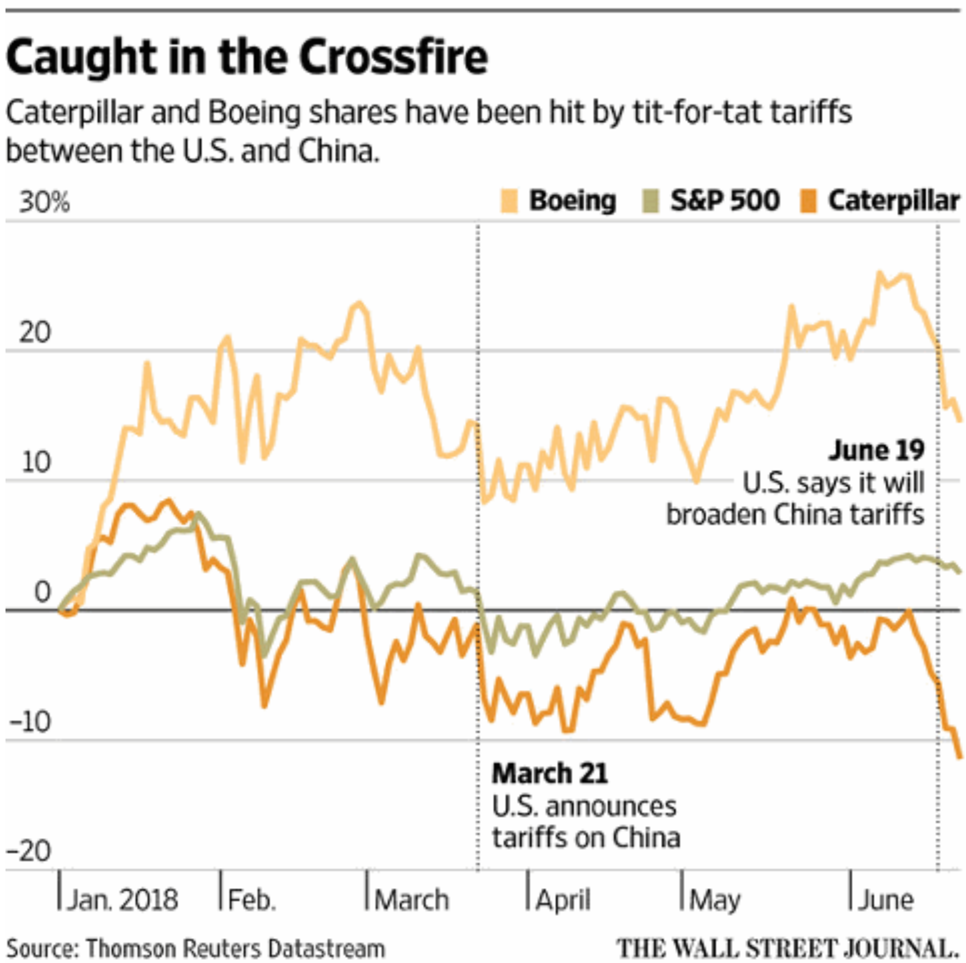
Measures of revenue exposure to China -- or of Chinese corporate exposure to the U.S. -- don't capture the complexity of modern manufacturing, either. U.S. company Qualcomm has microchips made for it in Taiwan, before they are sold into China to make mobile phones and shipped abroad. Even if China extended tariffs to U.S. chips, those made in Taiwan wouldn't be covered.

On the other hand, if the U.S. extends tariffs to consumer goods, then the suppliers to imported phones, including Apple's iPhone, could be hit. Ironically, a successful U.S. company is more exposed to possible U.S. tariffs on China than it is to Chinese tariffs on the U.S. Even worse is for chip makers who do produce in the U.S. and sell to China, as they might be hit twice, once if China levies a tariff on their chips, and once if the U.S. charges a tariff on the phone imported back from China.

UBS strategists who tried to isolate Asian stocks embedded in global supply chains also found little effect, until very recently.

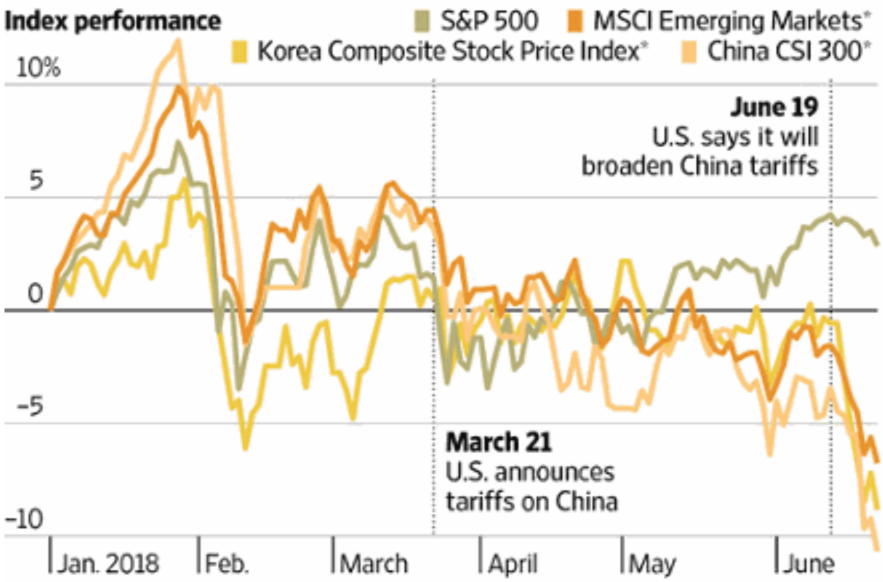
The biggest effect has instead been on wider markets and currencies. There has been no link between how much of an Asian company's sales come from the U.S. and its stock performance in local-currency terms, according to data from S&P Global Market Intelligence. But include the effect of currency moves, and U.S.-exposed Asian stocks have underperformed by about 10 percentage points, UBS found.

The simple rules of thumb -- sell China, sell Korea, sell emerging markets, prefer smaller to larger U.S. stocks and buy the safe-haven dollar and bonds -- have been working better than detailed analysis so far, in part because the prospects for a trade war are still so uncertain. If it becomes clear that new trade barriers are here to stay, understanding both the details of which companies will be hit and the knock-on effects on the economy will matter more.



Trade-Offs

China and its suppliers have been victims of the tariffs...



...but shares of S&P 500 companies with higher sales in China haven't all dropped since tariffs were announced in March.

Company	Percentage of revenue from China	Share-price change since March 21
Qorvo	51.8%	10.9%
Broadcom	53.6	5.5
Qualcomm	65.4	3.4
Micron Technology	51.1	-2.7
Wynn Resorts	73.3	-3.9
Skyworks Solutions	82.7	-8.9

*In U.S. dollars

Sources: FactSet (index performance); S&P Global Market Intelligence (companies)

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THE WALL STREET JOURNAL.
U.S. EDITION

Small-Cap Stocks Claim Higher Ground --- Rising dollar, concerns about weaker global growth lead investors to seek relative safety

By Jon Sindreu
902 words
22 June 2018
The Wall Street Journal
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B12
English

Investors are flocking to the shares of small companies as a looming trade war with China, a rising dollar and concerns about weaker global growth make these domestic-focused stocks more attractive than large-cap peers.

The S&P Small Cap 600 is on a tear, up 11% since the start of the year to a record, compared with a 2.8% gain for the **S&P 500**. The Russell 2000, another index of small U.S. companies, has gained 10%.

Small companies, as measured by market capitalization, tend to earn most of their money at home and are typically insulated form overseas turmoil.

"We continue to like small-cap equities because they have a more domestic focus, less impacted by trade or dollar fluctuations," said Angus Sippe, a fund manager at Schroders PLC, which has GBP 447 billion ($591.89 billion) under management.

Even in Europe, where the dollar's rise has benefited multinationals, the MSCI Europe Small Cap index is down 1.4% on the year through Wednesday, compared with a 5% fall for the broader MSCI Europe.

Medium-size companies have done better than their larger peers but have far underperformed smaller firms: In the U.S., the level of the S&P Small Cap 600 relative to the S&P Mid Cap 400 is the highest since 1998.

This past week, small companies widened their advantage, as trade tensions between the U.S. and China increased. On Monday, President Donald Trump called for a fresh round of tariffs on $200 billion of Chinese goods. Chinese officials have pledged to retaliate with tariffs on U.S. car makers, farmers and industrial companies.

Shares of U.S. multinationals such as Caterpillar Inc., Boeing Inc. and Deere & Co. were hit.

Analysts still need to work out how individual companies would be affected by a disruption in global trade, partly because many domestic-focused companies have globally exposed suppliers. But this is just one of the many factors that have benefited smaller companies in recent months.

Hopes of a prolonged synchronized period of global growth have lessened because of weaker economic data coming from Europe and China. Meanwhile, U.S. retail sales and consumer spending have continued to improve, suggesting that America's domestic economy has room to expand.

This has also boosted the U.S. dollar, reversing a stretch of weakness earlier in 2018. The WSJ Dollar Index, which measures the greenback against a basket of 16 currencies, is up 2.5% this year, making the foreign revenue of U.S. multinationals less valuable when converted back to dollars.

S&P 500 companies generate 38% of their income overseas, figures by data provider FactSet show, whereas for those in the S&P Small Cap 600 it is only 20%. Still, medium-size firms in the S&P Mid Cap 400 get 25% of their revenue from abroad -- not much more -- and their shares have risen far less.

"Sales growth is feeding through to the bottom," said Colin McLean, chief investment officer at SVM Asset Management. The Scottish firm has large stock allocations in small and medium-size companies around the developed world. "Investors have realized they've been underexposed to these stocks," he said.

Following last year's passage of U.S. tax cuts, a survey of small-business profitability in May hit its highest reading since records started in 1973, according to the National Federation of Independent Business. Views about business expansion were also the most optimistic in the survey's history.

Still, multinationals have reaped even larger benefits from the tax cuts. Earnings expectations for the **S&P 500** this year have been upgraded 9.2% since December, compared with 5.5% for the S&P Small Cap 600. Large companies also have a much bigger exposure to the technology sector, which has been the star of 2018.

This makes the rally in small-capitalization shares even more remarkable, although it has made them look more expensive. They now trade at almost 18 times the earnings they are expected to generate during the next 12 months, compared with 17 times for large-capitalization stocks, a larger gap than the average of the past decade.

David Lafferty, chief strategist at Natixis Global Asset Management, which manages about $900 billion, believes U.S. medium-size companies are more attractive than small ones, because they have greater liquidity and their valuations are similar to larger companies.

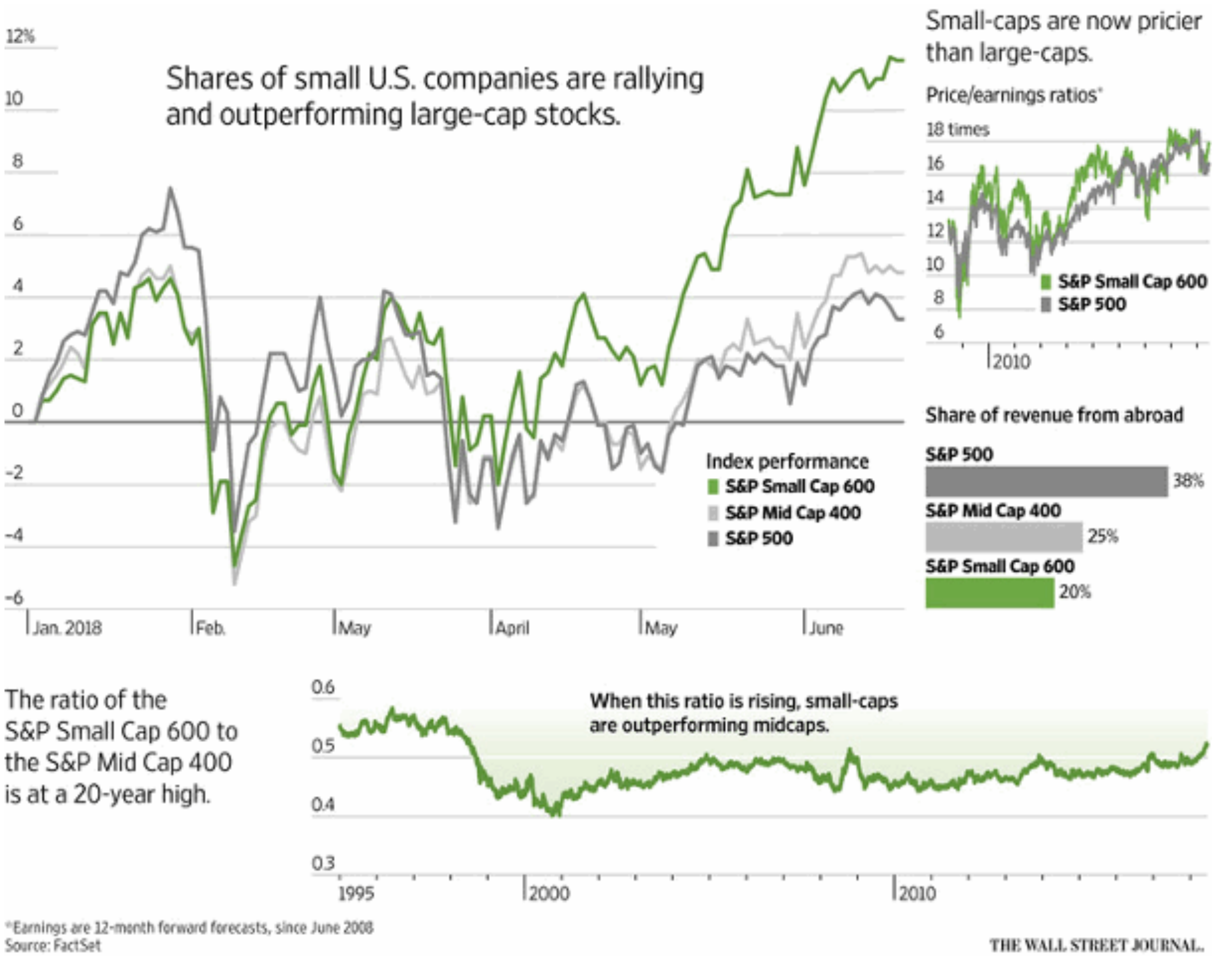
To be sure, preference for small-caps over the larger companies has swung up and down over the past decade. This is in contrast with the period between 2000 and 2005, when small-caps consistently gained ground.

Even in Europe, where the weakening euro has boosted multinationals' foreign revenue, some investors and analysts see domestic-focused firms as an attractive way to protect from the dangers of a widespread escalation in trade barriers.

For Roland Kaloyan, head of European equity strategy at Societe Generale SA, who believes the eurozone's soft patch will prove temporary, these shares are a good place for investors to park their money as interest rates go up.

"Small and medium-size companies were very leveraged five years ago, now they've deleveraged massively," he said.

Riva Gold contributed to this article.



Document J000000020180622ee6m00013

THE WALL STREET JOURNAL.
U.S. EDITION

Heard on the Street
Yen Again Proves to Be Haven in Storm

By Richard Barley
438 words
22 June 2018
The Wall Street Journal
J
B12
English

[Financial Analysis and Commentary]

It's been a stormy 2018 for markets, with **volatility** returning, trade tensions ratcheting higher and global growth proving less solid than expected. Investors looking for the financial equivalent of all-weather gear might find it in the Japanese yen.

The dollar's rise since April has been bruising. The euro is now down 3.3% for the year. But the yen, while well off its peaks, has proved more resilient and is still in positive territory, up 2.5% against the dollar, beating a string of its developed-market peers from the Canadian dollar to the Swedish krona.

That reflects its potentially unique appeal in today's world. The yen is well-known as a haven in times of trouble as the risk of turbulence causes yield-seeking Japanese investors to pull back from foreign assets, driving the currency up.

Moreover, the yen has the support of a big current-account surplus, forecast at 3.8% of gross domestic product in 2018 by the International Monetary Fund. That supports the currency when investors are fretting about countries that run deficits and need to attract capital. The yen has thus been resilient amid the trade clash between the U.S. and China.

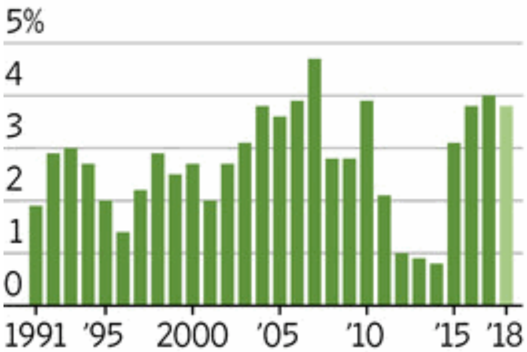
The yen might even benefit if the picture improves and global central banks feel more comfortable about tightening policy. The Bank of Japan is firmly at the back of the pack, but that means that there is room for the currency to rise if investors start to consider a move. Other currencies, like the euro and sterling, have shown that markets are very sensitive to this initial step, which can fuel appreciation. And structurally, there is reason to believe that the yen could be driven higher by Japan's aging population, which will need to sell foreign assets to fund spending, Morgan Stanley argues.

Importantly, the yen is seen as undervalued. Based on the average of a range of valuation measures, Deutsche Bank in June found it to be the cheapest of 31 currencies it had modeled.

One danger scenario for the yen is a world in which risk appetite surges alongside rising expectations of higher U.S. rates. That sounds like a stretch, because investors are wondering about risks related to the end of the financial cycle in light of the Federal Reserve's moves. The calm of 2017 seems unlikely to return swiftly. The yen is already in pole position this year and it looks likely to stay there.

Buoyant

Japan's current-account surplus as a share of gross domestic product



Note: 2018 is a forecast

Source: International Monetary Fund

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WSJ PRO CENTRAL BANKING

Economy

Banks Clear Tests | Kashkari: Slow Pace of Increases | Central Banks Go Separate Ways | Mexico Raises Rate | Torry's Take: Weak Inflation Expectations; The Wall Street Journal's central banking newsletter for Friday, June 22, 2018

1,612 words
22 June 2018
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WSJ Pro Central Banking
RSTPROCB
English

Torry's Take: Unfriending Weak Inflation Expectations

Big Banks Clear Fed's Stress Tests

Minneapolis Fed's Kashkari: Slow the Pace of Rate Increases

Central Banks Go Their Separate Ways

Bank of Mexico Raises Overnight Rate to 7.75%

Unfriending Weak Inflation Expectations

An all-star panel of central bankers met in Sintra, Portugal, on Wednesday to discuss some of the issues they face: moderate economic growth, low (or negative) interest rates and inflation.

One thing everyone agreed on was the importance of well-anchored inflation expectations.

"Today policy makers have a greater appreciation of the role expectations play in inflation dynamics and a clearer commitment to maintaining low and stable inflation," said Federal Reserve Chairman Jerome Powell.

Bank of Japan Gov. Haruhiko Kuroda talked about a "tenacious deflationary mind-set" in Japan.

"Consumers remain reluctant to accept price rises despite the improvement in the employment and income situation," which makes firms reluctant to raise prices, he said.

Reserve Bank of Australia Gov. Philip Lowe brought up a novel suggestion to combat the issue.

"Embrace social media, communicate better, make it very clear what inflation expectations should be, and the problem's kind of solved," he said.

Much as social media influencers build their brands through beach shots on Instagram and Twitter, central banks could try the same strategy to lift wage expectations.

For Mr. Lowe, a concern is that a 2% wage growth norm has become the standard in Australia, much as it has in economies like the eurozone.

"So 2% wage growth and reasonable labor productivity growth doesn't make for 2.5% inflation on a sustained basis," he said.

Lifting wage expectations is a better strategy than delivering more monetary stimulus to get inflation sustainably higher, he argued. What's more, the fact that small and large economies around the world are struggling with the same issues—including surprisingly slow wage growth—suggests global factors are at work. Those include increased competition due to globalization.

Businesses are so worried about diminishing margins or market share that they don't want to be the first to raise wages. Can a central bank help to break the cycle? At this point, a social media strategy may not be enough to reverse the attrition of collective bargaining or produce a meaningful shift in inflation expectations. But central bankers agree that the task is an important one.

"Anchoring inflation expectations was crucial and remains crucial," said European Central Bank President Mario Draghi.

Key Developments Around the World

Big Banks Clear Fed's Stress Tests

The Federal Reserve determined the largest U.S. banks were healthy enough to withstand a severe economic downturn and would continue lending during a crisis, as the industry posts record profits and prepares for a wave of regulatory relief. The Fed's "stress test" scenario for the 35 largest bank holding companies found the firms were "strongly capitalized" and would retain adequate capital levels in severely adverse conditions, according to the first round of results released Thursday by the central bank. The positive scorecard indicates most of the banks are likely to win the Fed's approval next week to increase dividends after a second round of tests that will determine whether the firms pass or fail the annual stress-test exercise.

Minneapolis Fed's Kashkari: Slow the Pace of Rate Increases

Federal Reserve Bank of Minneapolis President Neel Kashkari said Thursday the U.S. central bank should slow its pace of short-term interest-rate increases to give the labor market room to strengthen further. "We should really slow down," he said at an event in Minneapolis. "I don't see any signs of overheating, so why are we tapping the brakes on the economy?" Mr. Kashkari said the slow pace of wage growth is a sign that the labor market isn't as strong as the 3.8% unemployment rate might suggest. "Are we really at maximum employment? Until we really start to see that wage growth pick up, I don't think we are," he said.

Central Banks Go Their Separate Ways

Central banks in Europe on Thursday signaled different outlooks toward rate increases, suggesting the divergent paths of the world's largest central banks are gripping smaller ones too. The Bank of England held its benchmark interest rate steady at 0.5%, but officials said they expect economic growth in the U.K. to pick up in the months ahead following a soft start to the year, setting the stage for a rise in borrowing costs this summer. Norway's central bank also stayed on hold but said rates will probably go up in September. In contrast, the Swiss National Bank kept its key policy rate in deeply negative territory and signaled no forthcoming changes despite signs of healthy economic activity and slowly rising inflation, as the bank remains constrained by the actions of the European Central Bank.

U.K. Treasury, BOE Leaders Argue for Financial Services Agreement With EU

The U.K.'s top financial policy makers on Thursday made the case for an ambitious agreement on financial services between Britain and the European Union after Brexit, saying arrangements proposed by some in the EU don't go far enough. Treasury chief Philip Hammond and Bank of England Gov. Mark Carney said in back-to-back speeches at an annual dinner in London's financial district that a wide-ranging deal on financial services would benefit both the British and European economies. Their statements highlight how much of the future relationship between the U.K. and the EU is still unresolved almost two years after voters chose to exit from the EU in a referendum.

Bank of Mexico Raises Overnight Rate to 7.75%

The Bank of Mexicoraised interest rates Thursday, lifting borrowing costs in line with market expectations as a weaker Mexican peso threatens to derail this year's slowdown in inflation. The central bank increased the overnight interest-rate target by a quarter of a percentage point to 7.75%, its first move in three meetings. The decision to raise the rate was unanimous, and in line with expectations. "Some of the upside risks to inflation identified by the Central Bank have started to materialize," the bank said in a statement.

Ex-1MDB Investigator Appointed as Malaysia's Central Bank Governor

Malaysia has named Nor Shamsiah Mohd Yunus, a former central-bank official involved in an investigation into state-investment fund 1Malaysia Development Bhd., as governor of the regulator, a spokesman for the prime minister said Friday. The appointment confirms a Wall Street Journal report that Ms. Nor Shamsiah would replace Muhammad Ibrahim, who resigned as Bank Negara Malaysia governor earlier this month. He left following revelations that some $500 million used to buy land from the Finance Ministry was subsequently used to pay down the debt load at the fund, known as 1MDB.

Sunday

7:50 p.m. EDT

Bank of Japan releases summary of opinions for June 14-15 meeting

The Unintended Consequences of FOMC Press Conferences

"In an effort to increase transparency, the Chair of the Federal Reserve now holds a press conference following some, but not all, FOMC announcements," Charles Martineau writes in a research paper. "Evidence from **financial markets** shows that investors lower their expectations of important decisions on days without press conferences and that these announcements convey less price-relevant information. Using different proxies, we show that investors pay more attention to upcoming announcements with press conferences. This coordination of attention can reduce welfare in models of the social value of public information. Consistent with theories of investor attention, the market risk premium is larger on days with press conferences," he writes.

Japan's Yen: A Currency for All Seasons?

"Investors looking for the financial equivalent of all-weather gear might find it in the Japanese yen…The yen is well-known as a haven in times of trouble as the risk of turbulence causes yield-seeking Japanese investors to pull back from foreign assets, driving the currency up," Richard Barley writes for The Wall Street Journal. "The yen might even benefit if the picture improves and global central banks feel more comfortable about tightening policy. The Bank of Japan is firmly at the back of the pack, but that means that there is room for the currency to rise if investors start to consider a move…Importantly, the yen is widely seen as undervalued."

The number of Americans filing applications for new unemployment benefits fell for the fourth straight week in mid-June, signaling continued strength in the labor market heading into the summer.

Manufacturing activity across the mid-Atlantic continued to expand in June, but at a slower pace, the Federal Reserve Bank of Philadelphia said in a report Thursday.

The Conference Board Leading Economic Index continued its recent string of increases, rising by 0.2% in May.

Business activity in the eurozone picked up in June for the first month in five—a first sign that the currency area's economy may be shaking off a sluggish start to the year.

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

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

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The New York Times

Business/Financial Desk; SECTB
Trade Nerves Hit Car Makers; Tax Ruling Hits Online Sellers

By THE ASSOCIATED PRESS
681 words
22 June 2018
The New York Times
NYTF
Late Edition - Final
2
English

Car makers and technology and industrial companies fell Thursday as investors focused on the trade dispute between the United States and China, which could reduce company spending and earnings. The **Dow Jones Industrial Average** slipped for the eighth day in a row.

While investors generally do not expect a trade war between the United States and China, they remain sensitive to signs that rising tariffs and trade tensions will hurt the global economy and reduce corporate profits. This week they have received some signs that this is happening. On Thursday, German automaker Daimler said the tariffs China plans to put on cars imported from the United States will contribute to a small decline in earnings this year. Its stock fell 4.3 percent in Germany.

The previous day, Fed Chairman Jerome Powell said the Fed has heard about businesses holding off on hiring and spending in response to the trade conflicts. Kate Moore, global equity strategist for BlackRock, said that investors have been hoping that the Republican-backed corporate tax cut would encourage companies to hire more workers, boost pay, and expand their operations, but the uncertainty over tariffs is discouraging them from doing that.

''There's a fear that rising uncertainty around trade and tariffs is going to significantly affect investment decisions and hiring decisions, and potentially take some steam off of what has looked like a very strong expansion,'' she said.

The **Standard & Poor's 500**-**stockindex** slid 17.56 points, or 0.6 percent, to 2,749.76. The Dow fell 196.10 points, or 0.8 percent, to 24,461.70. The index has fallen 3.4 percent over the last eight days. Its last losing streak this long was in March 2017. The **Nasdaq composite** lost 68.56 points, or 0.9 percent, to 7,712.95.

Online retailers dropped following the Supreme Court ruling. For more than two decades, companies were not required to collect sales tax on online purchases that were made in a state where the company did not have a physical presence, such as a warehouse or office. States argued that those rules deprived them of billions of dollars in tax revenue, and traditional retailers said online sellers had an unfair advantage.

Overstock.com lost 7.2 percent to $36.15 and home goods site Wayfair gave up 1.6 percent to $114.28, while Amazon lost 1.1 percent to $1,730.22. Target gained 1 percent to $76.14, and Nordstrom added 1.8 percent to $52.78.

Energy companies skidded as investors expect OPEC to agree to a production increase at a meeting on Friday. Chevron fell 2.2 percent to $122.59, and Marathon Oil dropped 5.4 percent to $19.92.

United States crude dropped 0.3 percent to $65.54 a barrel in New York.

Intel fell 2.4 percent to $52.19 after its chief executive resigned. The world's largest chipmaker said Brian Krzanich is stepping down after the company learned he had a relationship with an employee. Intel said the relationship was consensual, but violated company policy.

Bond prices climbed. The yield on the **10**-**year Treasury** note fell to 2.90 percent from 2.94 percent. That helped stocks that pay big dividends including utilities and real estate investment trusts.

In other energy trading, wholesale gasoline lost 0.6 percent to $2.01 a gallon. Heating oil fell 1.8 percent to $2.07 a gallon. Natural gas rose 0.4 percent to $2.98 per 1,000 cubic feet.

Gold shed 0.3 percent to $1,267.20 an ounce.

The dollar fell to 109.90 yen from 110.40 yen. The euro rose to $1.1611 from $1.1579.

CHARTS: The **S**. **& P**. **500 Index**: Position of the **S**. **& P**. **500 index** at 1-minute intervals on Thursday. (Source: Reuters); Jobless Claims: Weekly number of people who have filed for unemployment benefits for the first time. (Source: Labor Department, via Reuters)

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THE WALL STREET JOURNAL.
U.S. EDITION

Fed Says Banks Can Bear the Worst --- First leg of stress test shows lenders are able to withstand a financial crisis

By Lalita Clozel and Telis Demos
1,155 words
22 June 2018
The Wall Street Journal
J
B1
English

The Federal Reserve determined the largest U.S. banks were healthy enough to withstand a severe economic downturn and would continue lending during a crisis, as the industry posts record profits and prepares for a wave of regulatory relief.

The Fed's "stress test" scenario for the 35 largest bank holding companies, which hold 80% of the assets at banks operating in the U.S., found the firms were "strongly capitalized" and would retain adequate capital levels in severely adverse conditions, according to the first round of results released Thursday by the central bank.

The positive scorecard indicates most of the banks are likely to win the Fed's approval next week to increase dividends after a second round of results that will determine whether the firms pass or fail the annual stress-test exercise, put in place after the 2008 crisis. However, Goldman Sachs Group Inc. and Morgan Stanley barely cleared one of the key regulatory minimums of the first round.

Thursday's results are the latest positive news for an industry that took years to dig itself out of the financial crisis and faced a tightened regulatory regime meant to prevent another period of financial turmoil. Congress and Trump-appointed regulators have taken steps to ease regulation and struck a cooperative tone with the industry, placing financial firms in a friendlier political climate at a time manufacturing, retail and other industries face uncertainty over U.S. trade policy.

"Despite a tough scenario and other factors that affected this year's test, the capital levels of the firms after the hypothetical severe global recession are higher than the actual capital levels of large banks in the years leading up to the most recent recession," Fed Vice Chairman for Supervision Randal Quarles said in a statement.

A senior Fed official said this year's economic scenarios were the toughest to date, a response to the strong economy. One-time accounting changes related to last year's tax law also handicapped some firms.

As a result, banks' capital levels fell closer to the regulatory minimums than they had in recent years. The banks' core common equity Tier 1 capital ratios collectively dropped as low as 7.9% during the scenario period, down from 12.3% in actual high-quality capital at the end of 2017. That is well above the 4.5% requirement. But it is still a smaller surplus than last year, when that ratio was 9.2%.

In certain cases, the cushion was much narrower. Goldman Sachs and Morgan Stanley, for example, just cleared their supplementary leverage ratios -- a measure that includes lending and derivative exposure relative to their capital levels. Goldman Sachs was 3.1% and Morgan Stanley 3.3%, compared with a 3.0% minimum.

Goldman Sachs appeared to be caught off guard by the results. In a statement, the bank said that its own capital models "diverge" from the Fed's, and it is "examining that divergence." Goldman also said its capacity to return capital "may be higher than this year's test would otherwise indicate."

A Morgan Stanley spokesman said in a statement that the stress-test results "may not be indicative of the capital distributions that we will be permitted to make" and said it would give more detail next week.

Firms conduct their own internal tests using the Fed's doomsday scenario. If after seeing the Fed's results, a company determines it is at risk for failing, it can take a "mulligan" and resubmit more conservative shareholder payouts.

The Fed won't take any direct action based on the results released Thursday. But they do signal how much capital the Fed will allow banks to return and could affect the size of the payouts that banks seek.

Banks have performed strongly in the initial round of stress tests for several years. In 2017, all firms also passed the more consequential second round, meaning the Fed didn't have to limit any of the banks' investor payouts.

Overall, the Fed calculated the largest U.S.-based bank holding companies would have loan losses of $429 billion under a hypothetical scenario that envisioned the U.S. unemployment rate rising to 10% and gross domestic product dropping 7.5%, with a steepening Treasury yield curve.

In contrast, banks are by many measures enjoying their strongest period in a decade. Boosted by a healthy economy and busy corporate clients, U.S. banks reported record profits for the first quarter, with $56 billion in net income, according to the Federal Deposit Insurance Corp.

The corporate tax cut in 2017 added about $7 billion to the bottom line for banks in the quarter. But even without that benefit, profit would still be at a record.

The biggest banks in particular are gobbling up market share from struggling overseas rivals and smaller U.S. lenders.

Thanks to a **volatile** market, stock-trading desks at the big five investment banks -- JPMorgan Chase & Co., Bank of America Corp., Citigroup Inc., Goldman Sachs and Morgan Stanley -- had their best start to a year in 2018 since the financial crisis.

The Fed exempted three banks that had submitted capital plans for the stress tests, thanks to the new banking law increasing a threshold for stricter regulatory supervision to $250 billion in assets from $50 billion. Those firms were CIT Group Inc., Comerica Inc. and Zions Bancorp. In the future, the Fed could also ease the stress tests for firms with $100 billion to $250 billion in assets.

Regulators also are working on other rule changes that would benefit big banks, including making it easier to comply with the Volcker rule, which bars banks from hedge-fund-like trading activities, and changing a capital requirement known as the enhanced supplementary leverage ratio, which requires the largest banks to maintain a minimum proportion of capital to assets.

Worries that rising short-term interest rates would squeeze banks are so far not being borne out. Americans still keep a huge percentage of their deposits at the biggest retail banks -- JPMorgan, Bank of America and Wells Fargo & Co. -- as those firms pay some of the lowest rates on savings accounts.

Banks continue to find ways to lend at higher rates. Commercial and industrial loan growth has picked up of late, and the U.S. market for loans to risky companies hit a trillion dollars for the first time this year.

The Fed's stress tests are released in two parts. On Thursday, the Fed assessed the health of the banking system as a whole and released "quantitative" results, or calculations showing how banks fared during hypothetical scenarios. On June 28 the Fed will say whether banks passed or failed, publishing a second version of the "quantitative" results.

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THE WALL STREET JOURNAL.
U.S. EDITION

U.S. News: Firms Get Chance For a Tax Break On Pension Plans

By Richard Rubin and Vipal Monga
558 words
22 June 2018
The Wall Street Journal
J
A5
English

Companies with underfunded pensions have a rare opportunity to score a tax break in the coming months.

Pension contributions made through mid-September can be deducted from income on tax returns being filed for 2017 -- when the U.S. corporate tax rate was still 35%. That means a company that contributes $100 million to its pension plan now can save $35 million in taxes, while a company contributing the same amount after the deadline would save just $21 million, based on the new 21% corporate tax rate.

With the deadline less than three months away, corporations are preparing to top off their pension plans to take advantage of the beneficial tax treatment. This one-time incentive is helping corporations close a pension-funding gap that topped $680 billion for S&P 1500 companies after the financial crisis, according to the consulting firm Mercer.

"There will be a bit of a race to get in underneath the wire," said Michael Moran, pension strategist for Goldman Sachs Asset Management. "We're seeing a lot of contributions pulled forward."

Shipping company United Parcel Service Inc., construction equipment-maker Deere & Co. and defense company Lockheed Martin Corp., among others, have made or announced contributions worth billions of dollars to their defined-benefit pension plans ahead of the cutoff date, citing the tax law among their reasons.

Boise Cascade Co., an Idaho-based lumber and building-materials company, said in earlier corporate filings it would contribute $2 million to its plans this year. The company is now considering contributing between $10 million and $20 million because of the tax benefit, said Wayne Rancourt, the company's finance chief.

"If we put $10 million into the plan, we'd deduct $3.5 million we'd otherwise pay in cash taxes," said Mr. Rancourt. "We may as well do it before the cutoff."

Kellogg Co. is weighing an additional pension contribution of between $200 million and $300 million, and Northrop Grumman Corp. said it was making a $250 million contribution.

Kellogg spokeswoman Kris Charles said the tax law didn't prompt the decision to consider a pension contribution but that the law did "encourage us to accelerate any such decision" to get the 2017 deduction. Northrop Grumman declined to comment.

Federal law allows companies to deduct contributions to defined-benefit pension plans from taxable income, lowering their tax bills. Companies must also keep pension plans well-funded -- meaning they hold enough assets to pay most, if not all, future benefits -- with some flexibility around timing.

Companies in the Russell 3000 index with defined-benefit plans could make more than $90 billion in contributions this year, ahead of the mid-September cutoff, according to an estimate from Chris Senyek, an accounting and tax policy analyst with New York-based Wolfe Research. That is more than the $81 billion they contributed last year, itself a 30% jump from 2016.

Companies with defined-benefit plans in the **S&P 500** carried obligations of $2.023 trillion as of June 12, but the value of the assets in the plans totaled only $1.811 trillion, leaving the plans 90% funded, according to consulting firm Aon PLC.

Tatyana Shumsky contributed to this article.

Document J000000020180622ee6m0001b

THE WALL STREET JOURNAL.

Markets
Gold Plumbs Fresh 2018 Lows as Rate Worries Continue; Prices have fallen more than 7% from their January peaks despite safe-haven buying; copper slides

By Amrith Ramkumar and David Hodari
599 words
21 June 2018
04:13 PM
The Wall Street Journal Online
WSJO
English

Gold prices fell to a fresh 2018 low on Thursday, continuing a prolonged retreat even as investor jitters over a potential trade war stoked **volatility** in other markets.

Front-month gold for June delivery declined 0.3% to $1,267.20 a troy ounce on the Comex division of the New York Mercantile Exchange, its fourth drop in the past five sessions and its lowest close since Dec. 20. Prices have fallen 7% from their January peaks despite anxiety over protectionist trade policies and inflation prompting some safe-haven buying, with gold traders instead more focused on the impact of higher interest rates.

The precious metal struggles to compete with yield-bearing assets like Treasurys as rates rise. On Wednesday, Federal Reserve Chairman Jerome Powell said at the European Central Bank's annual policy conference that sturdy U.S. economic growth has built a strong case for continuing to gradually lift interest rates. The comments came a week after the Fed raised rates for the second time this year and forecast two more increases for 2018.

On Thursday, the Bank of England's rate-setting committee voted to keep rates on hold by a margin of six to three, indicating a mildly more hawkish bias compared with its previous meeting.

"All of that is boosting interest-rate talk, and that is a negative for gold," said George Gero, managing director at RBC Capital Markets. "Gold is unable to compete with higher interest rates at the moment."

The recent **bearish** signals in the gold market mark a contrast from earlier in the year, when gold stayed above $1,350 and some bulls called for prices to pierce $1,400 for the first time since 2013. Now, some analysts are betting prices could fall further if they get below $1,250 and economic growth in the U.S. remains strong.

Some investors are also wondering whether the recent rally in gold, which had its best year since 2010 a year ago, might come to an end. Mr. Gero noted that some money managers have recently been selling gold to cover margin calls on other assets, with other commodities also falling on trade and interest-rate fears.

"As the commodity accounts started to decrease, they've had to raise cash, and selling gold has been one of the easiest ways to do that," he said.

The dollar has stabilized on the back of escalating trade friction between the U.S. and China, making gold more expensive for overseas buyers. On Thursday, the WSJ Dollar Index, which tracks the dollar against a basket of 16 other currencies, edged down 0.3% from its highest level in nearly a year.

While a trade war would sting U.S. companies, their losses would be milder than those in other countries, according to Simona Gambarini, a commodities economist at Capital Economics.

Gold typically climbs in the wake of increased geopolitical tensions, but "the headwinds from Fed tightening are stronger than the potential positive impact on gold prices of trade tensions," Ms. Gambarini said.

Among base metals, front-month copper for June delivery edged down 0.7% to $3.0250 a pound. Prices have fallen 8.1% from their year-to-date highs hit earlier this month, hurt by unease over potentially growth-hindering trade policies.

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

Document WSJO000020180621ee6l0038p

THE WALL STREET JOURNAL.

U.S. Markets
Markets

U.S. Stocks Retreat as Trade Tensions Linger; Shares of auto makers slide after Daimler issues profit warning

By Danielle Chemtob and Christopher Whittall
628 words
21 June 2018
05:49 PM
The Wall Street Journal Online
WSJO
English

Corrections & Amplifications

The **Dow Jones Industrial Average** was headed Thursday toward its longest losing streak since March 2017. An earlier version of this article incorrectly said the index was on course to post its longest losing streak since late March.

The **Dow Jones Industrial Average** fell Thursday, notching its longest streak of consecutive declines in more than a year as trade friction between the U.S. and China weighed on stocks.

The consequences of escalating trade tensions became clearer after German auto maker Daimler AGissued an unexpected profit warning late Wednesday, saying Chinese retaliatory import duties on vehicles built in the U.S. would crimp sales and earnings.

The announcement pushed down shares of auto makers and other trade-sensitive stocks around the world and gave investors a glimpse of how President Donald Trump's moves to enact protectionist trade policies could affect corporate profits. The Dow industrials declined nearly 200 points to post an eighth consecutive session of losses, the longest run of daily declines since March 2017.

"If we continue to see other companies start to warn that the trade war—trade tariffs—start to have an impact on earnings, that would be bad for all stocks and really bring market sentiment down," said Brant Houston, managing director and portfolio manager at CIBC Atlantic Trust.

The Dow industrials declined 196.10 points, or 0.8%, to 24461.70. The **S&P 500** fell 17.56 points, or 0.63%, to 2749.76. The tech-heavy **Nasdaq Composite** shed 68.56 points, or 0.9%, to 7712.95 in its worst day since April.

Shares of Ford dropped 16 cents, or 1.3%, to $11.71, and General Motors lost 83 cents, or 2%, to 41.12.

Rising tariffs between the U.S. and trading partners such as China and Europe are only part of the story, some analysts said. The biggest threat to car makers is what happens to the North American Free Trade Agreement between the U.S., Canada and Mexico, said Philippe Houchois, an equity analyst at Jefferies.

"The longer-term risk is to what extent it affects what car companies have been doing for the last two decades in terms of globalizing their supply chains," he said.

Shares of energy companies also struggled Thursday as officials from major oil-exporting countries reportedly neared a deal to increase crude output by one million barrels a day. The **S&P 500** energy sector fell 1.9%, with Chevron declining 2.70, or 2.2%, to 122.59. Exxon Mobil lost 76 cents, or 0.9%, to 79.69.

Shares of e-commerce companies also slumped after the Supreme Court ruled Thursday that states can require online merchants to collect sales tax. Shares of Amazon.com fell 19.86, or 1.1%, to 1730.22 and eBay declined 1.25, or 3.18%, to 38.01.

But traditional retailers could benefit from the ruling, said Sandy Villere, portfolio manager of the Villere Balanced Fund. Target rose 75 cents, or 1%, to 76.14, while Best Buy added 1.37, or 1.8%, to 77.23.

"I think it could level the playing ground a little bit between some of the internet retailers versus bricks-and-mortar," Mr. Villere said.

Technology companies also traded lower, with shares of Intel sliding 1.27, or 2.4%, to 52.19. The company's chief executive resigned after the chip maker determined he violated company policy during a past, consensual relationship with an Intel employee.

Shares investors typically buy in times of **volatility** rose Thursday, with the **S&P 500**'s utilities and real-estate sectors gaining 0.3% and 0.6%, respectively.

Elsewhere, the Stoxx Europe 600 shed 0.9%, closing at its lowest value since April.

The Shanghai Composite Index fell 1.4%, while Japan's Nikkei Stock Average gained 0.6%.

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THE WALL STREET JOURNAL.

World

Iran Throws Wrench Into OPEC Plan to Lift Production; Saudi minister says there is broad support for proposal to raise crude output by one million barrels a day

By Summer Said, Benoit Faucon and Christopher Alessi
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21 June 2018
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The Wall Street Journal Online
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English

VIENNA—Iran said late Thursday it was still opposed to a deal to lift oil output, fraying a sense of consensus among OPEC members and putting it at loggerheads with Saudi Arabia, the cartel's de facto leader.

The surprise move—after signals throughout the day that Iran was warming to an agreement—heightens uncertainty about whether Saudi Arabia can maintain discipline among members of the Organization of the Petroleum Exporting Countries as it seeks to dole out more oil to thirsty global markets. Riyadh has led OPEC in a pact with Russia and a handful of other non-OPEC members in whittling down a large surplus of crude that has kept prices low for years.

That deal, reached in 2016, displayed an uncommon level of compliance among global producers. Now, with Iran openly rebelling, that sense of discipline is threatened.

Saudi Arabia, its Persian Gulf allies and Russia can move ahead with an increase without Tehran. But OPEC decisions are usually unanimous. Disarray inside the group could signal to markets the tightly coordinated oil policy among the Riyadh- and Moscow-led group is coming apart.

Representatives of other influential OPEC members, including Nigeria and Iraq, in comments to reporters after a late-night technical meeting Thursday, said they backed a plan pushed by Saudi Energy Minister Khalid al Falih to boost output by one million barrels day. Mr. Falih said he had support from an "overwhelming majority" for the one-million-barrel increase.

Mr. Falih also said a working group of OPEC members and nonmembers had agreed to back the proposal. OPEC meets Friday to make a final decision.

Iran can't raise output on its own, partly because new U.S. sanctions are likely to keep buyers away. But Iran's intransigence would challenge Riyadh's authority in the group. Analysts and officials have worried that could lead to a free-for-all among other producers, who might be tempted to open the taps to compete for market share—driving down prices.

"There still some time left to negotiate until the meeting starts on Friday, but (it) is likely to be a tough one," said Giovanni Staunovo, commodity strategist at UBS.

OPEC meetings are often contentious right down to the last minute, and Iran in particular has frequently clashed with Saudi Arabia over output decisions. Tehran has used this OPEC meeting to accuse Riyadh of bowing to U.S. demands to pump more oil. Washington has asked Saudi Arabia to provide more oil amid the new sanctions on Iran, according to people familiar with the matter. President Donald Trump has tweeted that prices are too high and has blamed OPEC.

Earlier in the day, a relatively smooth meeting looked possible. Iran's oil minister arrived early in the week vowing to reject any output increase. But by Thursday officials familiar with the Iranian delegation's thinking expected a compromise. Mr. Falih floated the plan to lift daily output by one million barrels.

That was more than Riyadh had originally wanted but far less than the 1.5 million barrels a day Moscow was seeking. The plan was enough to convince traders more oil was coming to market and sent crude prices down.

Hours later, though, Iran's Oil Minister Bijan Zanganeh said he was still far from convinced a deal was close. "I don't think there will be an agreement," he told reporters.

Mr. Falih and Russian counterpart Alexander Novak have said they are willing to ease up on the 2016 output cut the two countries orchestrated. That pact reduced output by about 2% of global production at the time—or about 1.8 million barrels a day.

More recently, though, it has led to sharply higher crude prices and complaints from consumer countries like the U.S. and Asian buyers. OPEC has traditionally worried that too-high **oil prices** could curb demand.

On paper, the plan circulated by Mr. Falih on Thursday is bigger than what he and other OPEC allies have floated recently in response to Russia's entreaties. As recently as Wednesday, he was pushing a plan to increase the group's output by 500,000 barrels a day, according to people familiar with the matter.

But behind the scenes, people familiar with the matter say, Thursday's proposal is more in line with what the Saudis and allies have been advocating all along. Because of output constraints, the current proposal would eventually amount to just 600,000 barrels a day of additional crude, they say.

The Saudi plan, officials have previously said, would consist of a first boost by OPEC's 14 member states and a group of 10 Russia-led allies amounting to about 500,000 barrels a day in the third quarter. This would then be followed by the same amount in the fourth quarter.

But many members of the group are limited in how much they can lift output. Several are pumping flat out, while a few OPEC members, including Libya, Venezuela and Iran, are dealing with output constraints. Rebels have attacked Libyan ports, reducing exports. An acute economic crisis has hit Venezuelan production. U.S. sanctions threaten to bottle up Iranian crude.

That all means the OPEC and non-OPEC group would only really be adding about 600,000 barrels a day in new crude output, people familiar with the matter said.

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THE WALL STREET JOURNAL.

Markets

Big Banks Clear Fed's Stress Tests; Federal Reserve releases first round of results of annual exams assessing banks' health; second part is next Thursday

By Lalita Clozel and Telis Demos
1,453 words
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The Federal Reserve determined the largest U.S. banks were healthy enough to withstand a severe economic downturn and would continue lending during a crisis, as the industry posts record profits and prepares for a wave of regulatory relief.

The Fed's "stress test" scenario for the 35 largest bank holding companies, which hold 80% of the assets at banks operating in the U.S., found the firms were "strongly capitalized" and would retain adequate capital levels in severely adverse conditions, according to the first round of results released Thursday by the central bank.

The positive scorecard indicates most of the banks are likely to win the Fed's approval next week to increase dividends after a second round of results that will determine whether the firms pass or fail the annual stress-test exercise, put in place after the 2008 crisis. However, Goldman Sachs Group Inc. and Morgan Stanley barely cleared one of the key regulatory minimums of the first round.

Thursday's results are the latest positive news for an industry that took years to dig itself out of the financial crisis and faced a tightened regulatory regime meant to prevent another period of financial turmoil. Congress and Trump-appointed regulators have taken steps to ease regulation and struck a cooperative tone with the industry, placing financial firms in a friendlier political climate at a time manufacturing, retail and other industries face uncertainty over U.S. trade policy.

"Despite a tough scenario and other factors that affected this year's test, the capital levels of the firms after the hypothetical severe global recession are higher than the actual capital levels of large banks in the years leading up to the most recent recession," Fed Vice Chairman for Supervision Randal Quarles said in a statement.

A senior Fed official said this year's economic scenarios were the toughest to date, a response to the strong economy. One-time accounting changes related to last year's tax law also handicapped some firms.

As a result, banks' capital levels fell closer to the regulatory minimums than they had in recent years. The banks' core common equity Tier 1 capital ratios collectively dropped as low as 7.9% during the scenario period, down from 12.3% in actual high-quality capital at the end of 2017. That is well above the 4.5% requirement. But it is still a smaller surplus than last year, when that ratio was 9.2%.

In certain cases, the cushion was much narrower. Goldman Sachs and Morgan Stanley, for example, just cleared their supplementary leverage ratios—a measure that includes lending and derivative exposure relative to their capital levels. Goldman Sachs was 3.1% and Morgan Stanley 3.3%, compared with a 3.0% minimum.

Goldman Sachs appeared to be caught off guard by the results. In a statement, the bank said that its own capital models "diverge" from the Fed's, and it is "examining that divergence." Goldman also said its capacity to return capital "may be higher than this year's test would otherwise indicate."

A Morgan Stanley spokesman said in a statement that the stress-test results "may not be indicative of the capital distributions that we will be permitted to make" and said it would give more detail next week.

Firms conduct their own internal tests using the Fed's doomsday scenario. If after seeing the Fed's results, a company determines it is at risk for failing, it can take a "mulligan" and resubmit more conservative shareholder payouts.

The Fed won't take any direct action based on the results released Thursday. But they do signal how much capital the Fed will allow banks to return and could affect the size of the payouts that banks seek.

Banks have performed strongly in the initial round of stress tests for several years. In 2017, all firms also passed the more consequential second round, meaning the Fed didn't have to limit any of the banks' investor payouts.

Overall, the Fed calculated the largest U.S.-based bank holding companies would have loan losses of $429 billion under a hypothetical scenario that envisioned the U.S. unemployment rate rising to 10% and gross domestic product dropping 7.5%, with a steepening Treasury yield curve.

In contrast, banks are by many measures enjoying their strongest period in a decade. Boosted by a healthy economy and busy corporate clients, U.S. banks reported record profits for the first quarter, with $56 billion in net income, according to the Federal Deposit Insurance Corp.

The corporate tax cut in 2017 added about $7 billion to the bottom line for banks in the quarter. But even without that benefit, profit would still be at a record.

The biggest banks in particular are gobbling up market share from struggling overseas rivals and smaller U.S. lenders.

Thanks to a **volatile** market, stock-trading desks at the big five investment banks— JPMorgan Chase & Co., Bank of America Corp., Citigroup Inc., Goldman Sachs and Morgan Stanley—had their best start to a year in 2018 since the financial crisis.

The Fed exempted three banks that had submitted capital plans for the stress tests, thanks to the new banking law increasing a threshold for stricter regulatory supervision to $250 billion in assets from $50 billion. Those firms were CIT Group Inc., Comerica Inc. and Zions Bancorp. In the future, the Fed could also ease the stress tests for firms with $100 billion to $250 billion in assets.

Regulators also are working on other rule changes that would benefit big banks, including making it easier to comply with the Volcker rule, which bars banks from hedge-fund-like trading activities, and changing a capital requirement known as the enhanced supplementary leverage ratio, which requires the largest banks to maintain a minimum proportion of capital to assets.

Worries that rising short-term interest rates would squeeze banks are so far not being borne out. Americans still keep a huge percentage of their deposits at the biggest retail banks—JPMorgan, Bank of America and Wells Fargo & Co.—as those firms pay some of the lowest rates on savings accounts.

Banks continue to find ways to lend at higher rates. Commercial and industrial loan growth has picked up of late, and the U.S. market for loans to risky companies hit a trillion dollars for the first time this year.

The Fed's stress tests are released in two parts. On Thursday, the Fed assessed the health of the banking system as a whole and released "quantitative" results, or calculations showing how banks fared during hypothetical scenarios. Next week—on June 28—the Fed will say whether banks passed or failed, publishing a second version of the "quantitative" results reflecting the individual capital plans of each bank and in some cases evaluating "qualitative" issues such as weaknesses in risk-management.

The qualitative release next week remains a potential tripping wire for large banks that are well-capitalized but have faced rebukes from regulators on other aspects of their operations, including consumer harm.

Vulnerable banks may include the U.S. operations of Deutsche Bank AG, which was designated about a year ago by the Fed as "troubled," or Wells Fargo & Co., which is still weathering regulatory punishments two years after the customer-abuse scandal broke, including a $1 billion fine and limitations on its ability to expand its banking business.

Deutsche Bank exceeded the Fed's stressed-scenario minimums. It has struggled in past years to pass the qualitative portion of the tests, even for just part of its U.S. business. This is the first year Deutsche Bank's full U.S. holding company has been subject to the tests, raising uncertainty among investors and analysts about next week's results.

The stress tests were first conducted in 2009 to help convince investors that the banking system wasn't about to collapse. Early on, they were a nail-bitingly public process for banks that was scrutinized by the public and investors for signs of weakness.

But today, the tests appear less relevant to market observers.

"There's just not that much excitement any more," said Michael Alix, a partner at consulting firm PwC and a former official at the Federal Reserve Bank of New York. "It's become more the expectation that institutions are going to pass."

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International New York Times

business

Trump's Ace in the Hole in Trade War: A Strong Economy

By NELSON D. SCHWARTZ
1,349 words
21 June 2018
International New York Times
INHT
English

The American economy has picked up speed and is now on course to expand this year at the fastest rate in more than a decade. That acceleration gives President Trump a stronger hand as he contemplates more tariffs and takes an increasingly confrontational approach with China, Canada, Mexico and other trading partners.

Economists have raised their growth estimates for the second quarter to an annualized rate of nearly 5 percent, more than double the pace of the previous period. Some economists say the figure could hit 3 percent for the full year, a level last reached in 2005.

As growth slows in Europe, China, Japan and elsewhere, the United States finds itself at the top of the global economy. The United States is also less exposed to the fallout from an escalating trade war since it does not rely on exports as much as other countries. It all gives Mr. Trump leverage with world leaders, potentially forcing them to make concessions.

But his threats could also backfire. Economists warn that the president's clout is limited and that his attacks on the trading system could dampen the outlook not just in other countries but also domestically.

"If you have the strongest economy in years, then the trade shock appears manageable," said Gregory Daco, head of United States economics at Oxford Economics. "However, with growth peaking, the trade shock will become more intense. With a global backdrop that is not improving anymore, we have to be careful about the back half of 2018 and 2019."

In July, the recovery will reach the nine-year mark, making it one of the longest in modern history. But for much of that time, the engines of the economy were rarely synchronized. When consumers were spending at a healthy clip in 2015 and 2016, business investment lagged as energy companies scaled back or abandoned projects in response to a sharp drop in **oil prices**.

All that has changed in recent months. Now, the different parts of the economy appear to be operating as one well-oiled machine. Consumer spending rebounded after a soft start to the year, with retail sales in May rising by a robust 0.8 percent, double what analysts had forecast.

"We have a very strong economy, and if the trade negotiations are successful, it'll be even stronger," said Kevin Hassett, chairman of the White House Council of Economic Advisers. He added that the president was "impatient to fix broken policies," with trade at the top of the list after last year's tax overhaul and deregulation effort.

The trade deficit, often cited by the White House as a vulnerability, narrowed in April, further bolstering economic activity in the second quarter. Strong April orders for fabricated metal, computers and other goods used in production also helped, as did a buildup in inventory as businesses restocked shelves. Such additions to inventory barely had an impact on growth in the first three months of the year, but could contribute nearly a full percentage point in the second quarter.

Increased government spending is providing added propulsion. The two-year budget deal reached in Congress in February added $300 billion in new government spending that is starting to flow into the economy. "It's something of a sugar high, but it feels good," said Diane Swonk, an economist with Grant Thornton in Chicago.

Taken together, these factors have compelled economists to re-evaluate the economy's tempo. At the beginning of May, Macroeconomic Advisers, a forecasting firm based in St. Louis, estimated growth of 3 percent in the second quarter. By mid-June, it was putting the figure at 4.5 percent. The Federal Reserve Bank of Atlanta's GDPNow model is even more upbeat at 4.7 percent.

But the good news may not last. While Ms. Swonk expects a 3 percent expansion for the full year, she added, “This likely will be the peak growth for this cycle.”

Contributing to that view is the rise in interest rates as the Federal Reserve gradually withdraws the easy credit that persisted for much of the recovery. “The headwinds are mounting,” Ms. Swonk said.

And then there are fears of an expanding trade war. Tariffs could hurt the American economy by stoking inflation without increasing wages.

Trade wars won’t sharply curtail economic activity, unless they cause businesses to lose confidence, said Spencer Dale, chief economist for BP, the energy giant. The bigger problem, he said, is that trade wars could “eat away at trend growth” by reducing G.D.P. by a fraction of a percent a year. That might not seem meaningful in any given year, but compounded over a decade or two, it could leave the economy noticeably short of what it might otherwise have achieved.

The Fed chairman, Jerome H. Powell, has also noted those risks. “Changes in trade policy could cause us to have to question the outlook,” he said on Wednesday at a European Central Bank conference in Portugal.

Still, the United States remains more insulated from a trade shock than other countries. Exports account for just 12 percent of American gross domestic product. That’s the lowest share among the 35 members of the Organization for Economic Cooperation and Development, a group of industrialized countries. By contrast, the figure is 31 percent in Canada, 37 percent in Mexico and 44 percent in the European Union.

In the United States, consumer spending accounts for nearly 70 percent of G.D.P. And recent surveys and other data show that people are **bullish** about the economy’s trajectory, according to Ian Shepherdson of Pantheon Macroeconomics. Owners of small businesses are also confident — about their own prospects and about the overall economy.

When Mr. Shepherdson put out a note to clients on May 14 highlighting the possibility of 5 percent growth in the quarter, he was quick to add that his forecast looked outlandish. “I was being tongue in cheek, looking at what would happen if everything goes right,” he said. “But it’s become more like the base case.”

Despite the improving consensus, Mr. Shepherdson said the quarter’s pace “is not sustainable,” but he does expect consumer spending to be solid in the second half of the year.

Sean McCartney, an executive vice president at Radial, a fulfillment and logistics business, agrees, and he’s putting his money to work. Radial will hire about 24,000 temporary workers later this year for the company’s fulfillment centers, call centers and warehouses to prepare for back-to-school demand and the holiday shopping season. That’s up by roughly 1,000 from last year.

“This year is shaping up to be strong, the strongest since the recovery began,” Mr. McCartney said. E-commerce companies represent most of Radial’s business, and the company has expanded its footprint to ensure faster deliveries.

Many of its operations are in the middle of the country, in states like Ohio and Kentucky, with plentiful transportation links enabling them to reach both coasts.

To attract new workers and keep existing ones, Radial has been offering spot raises of $1 an hour for temporary positions in some cities, on top of the typical $12-an-hour average for Radial’s network of sites.

“We have hundreds of open positions,” Mr. McCartney said. “We definitely could hire more than we have.”

PHOTOS: Above, Boyds department store in Philadelphia. Consumer spending is exceeding forecasts. Right, a factory in Toronto. Canada relies more on exports more than the U.S. does. (PHOTOGRAPHS BY MICHELLE GUSTAFSON FOR THE NEW YORK TIMES; MARK BLINCH/REUTERS) (A17) CHARTS: The Economy Accelerates: REAL ECONOMIC GROWTH; RETAIL SALES (Sources: Commerce Department; Federal Reserve Bank of Atlanta; Census Bureau) (A17)

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THE WALL STREET JOURNAL.
U.S. EDITION

Retailers Defy Predictions of Their Demise

By Akane Otani
743 words
21 June 2018
The Wall Street Journal
J
B1
English

Everyone knows that Amazon.com has left retailers for dead. Just don't tell investors in some stocks of big store chains.

Shares of retailers are enjoying their biggest rally in years, an unexpected turnaround fueled by strong earnings, buoyant consumer confidence and a nationwide shopping spree.

The SPDR S&P Retail ETF is up 11% this year, more than tripling the **S&P 500**'s 3.5% gain. During Tuesday's market rout, the retail ETF fell less than the broader market. Share prices of department stores such as Macy's Inc. and Dillard's Inc. have risen more than 55% this year, even edging out Amazon.com Inc.'s 50% advance.

The sector's big gains represent an abrupt reversal from previous years, when competition from e-commerce giants like Amazon pounded many traditional retailers, from teen apparel to auto-accessory makers. The S&P Retail Index underperformed the **S&P 500** in four of the past five years.

Retail's sudden resurgence is sparking a debate over whether flush-feeling consumers can keep the rally going, or if a series of temporary factors boosted the stocks in a way that is likely to fade in the second half of the year.

Some investors have found reasons to be optimistic. For one, many retailers posted better-than-expected earnings reports: Macy's, Home Depot Inc. and Walmart Inc. all reported same-store sales rising in the latest quarter. That has lifted share prices for some stocks whose valuations had fallen to single digits last year.

Retail sales -- a measure of what Americans spend on everything from cars to clothing to sporting goods -- rose 5.9% from a year earlier, according to the Commerce Department. Analysts attributed the gains, which marked the biggest one-month jump since November, to a combination of rising wages, low unemployment and tax cuts that have left many Americans with more money to spend -- all things that retailers hope will keep business at their stores humming.

"It is nice to see that consumer confidence is improving . . . and that [consumers are] voting on apparel certainly is a help in the industry," said Fran Horowitz-Bonadies, chief executive officer of Abercrombie & Fitch Co., on the firm's earnings call at the start of the month.

Still, some analysts caution that retail's recent rebound could be temporary, driven heavily by factors such as one-time gains from the U.S. tax overhaul rather than fundamental changes in the industry.

"Retail has received a second wind from the tax cuts, which we think will ultimately fade," said Morgan Stanley analysts in a recent report. Some analysts are forecasting a steep deceleration in earnings growth for the sector in coming months. "If so, look for the stocks to roll over as well," the Morgan analysts wrote.

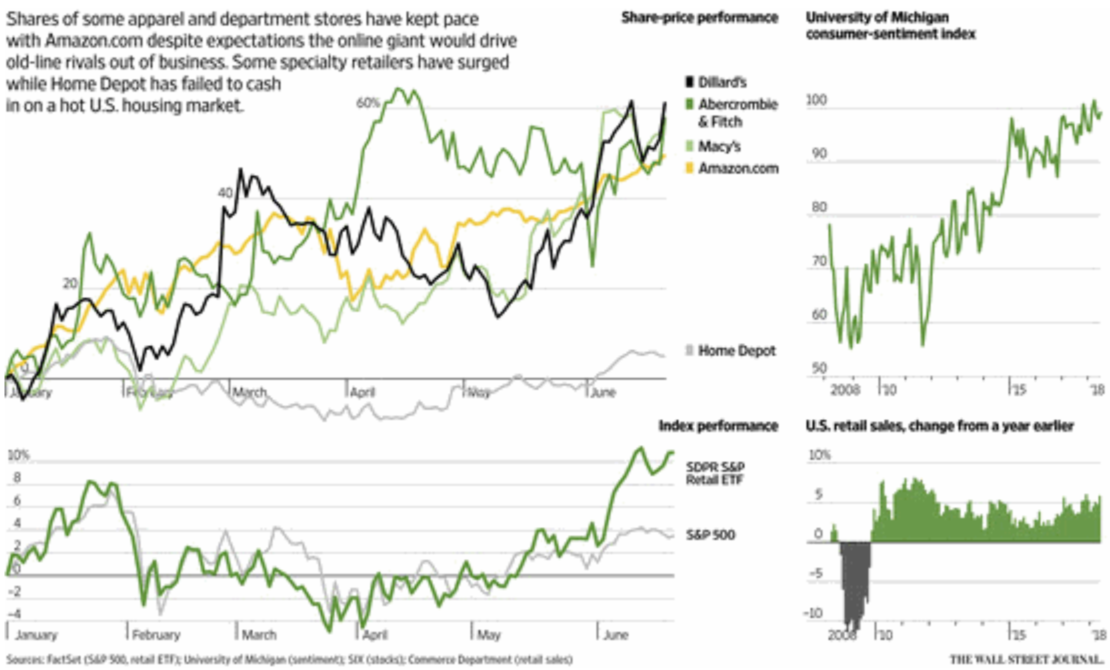
Other analysts point to the dollar as a reason why the rally may not last. While many retailers cited dollar weakness as boosting spending by foreign customers during the latest quarter, the currency has since rebounded. Further dollar gains would make retailers' goods more expensive to customers abroad, potentially slowing sales at companies with large multinational presences.

"People are saying, OK, these guys aren't going away now, so after the tremendous pressure we saw in 2016 and 2017, a number of those names are doing better," said Jim Tierney, chief investment officer of concentrated U.S. growth at AllianceBernstein.

He remains cautious on retail in the longer term, likening its recent performance to a "dead cat bounce": a short rebound following a sharp and prolonged selloff.

Macy's, which fell 30% in 2017 even as the **S&P 500** jumped 19%, is up 57% this year after closing dozens of stores while sales at its remaining stores have rebounded. In May, its same-store sales surpassed analysts' estimates, thanks to a pickup in spending by international tourists, revamped shoe and fine jewelry departments and customers' increased spending on full-priced goods.

Specialty retailers also have fared well. Dick's Sporting Goods Inc. is up 28% after losing 46% in 2017, buoyed by reports showing profits growing even as its hunting business suffered following a decision to tighten gun policies. Teen retailers Abercrombie & Fitch and American Eagle Outfitters Inc., which both posted better-than-expected same-store sales for the latest quarter, are up 58% and 31%, respectively.



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THE WALL STREET JOURNAL.
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U.S. News -- Capital Account: U.S. Turns From Global Uniter to Disrupter

By Greg Ip
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21 June 2018
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The western world has seen plenty of division and conflict before. But in the past the U.S. was the stabilizer, seeking to align its interests and those of its partners. Today, it is the destabilizer, driven by a belief that its interests and the world's are at odds.

The relatively buoyant **stock market** and economy might suggest this doesn't matter. Tariffs announced to date are tiny relative to gross domestic product and quantitatively matter much less than tax cuts. Even the most committed free traders admit protectionism does its damage slowly.

But the disconnect between global discord and American prosperity may be fragile. Economies are accident-prone: Natural disasters, wars and financial crises come out of nowhere, and global cooperation has often served to contain their damage. Strains are already apparent, in the European Union, on the Mexico-U.S. border, and in emerging markets. Solving these or any other crises gets harder the more mistrust grows between the U.S. and the rest of the world.

President Donald Trump's antagonism toward U.S. allies and trading partners reflects a belief that they are free riders on the U.S. military and economy. And it is true that since World War II the U.S. has borne a disproportionate share of the cost of sustaining military alliances and free trade.

But to suggest other countries sacrifice nothing to help the U.S. ignores plenty of military and economic history. After al Qaeda attacked the U.S. in 2001, Britain, Canada, Germany, France, Italy, Spain and the Netherlands each sent thousands of troops to Afghanistan. More than 800 died. Britain's contribution to the U.S.-led invasion of Iraq in 2003 cost Prime Minister Tony Blair heavily in political support and reputation.

It was the U.S. that, starting in the 1990s, prodded other countries to adopt safeguards against money laundering. After 9/11, that infrastructure proved invaluable in the fight against terrorism financing, said Daniel Drezner, a political scientist at Tufts University. The sanctions that Barack Obama, prodded by a Republican Congress, pushed the world to adopt forced Iran to accept curbs on its nuclear program (whether Mr. Obama used that leverage effectively is another question). Germany has suffered much more, economically, than the U.S. for the sanctions imposed on Russia for its annexation of Crimea.

On economics, too, other countries have often bent to U.S. priorities. In 1978 West Germany agreed to stimulate its economy with deficit spending to help the U.S. narrow its trade deficit. In 1985 the Group of Seven advanced economies jointly intervened to bring down the dollar to narrow the U.S. trade deficit. Japan paid a steep price: It countered the strong yen with low interest rates that produced the bubble economy and its collapse. During the global financial crisis of 2008, other countries heeded U.S. entreaties to stimulate their economies and thus prop up demand, while the Federal Reserve teamed up with other central banks to pump dollars into foreign banks and prevent fire sales of mortgage-linked securities.

While nothing comparable looks likely now, there are plenty of scenarios in which bad blood between the U.S. and others could aggravate a crisis. Arguably, the southern border offers one example. Mexico could stem the tide of Central American migrants reaching the U.S. border by requiring a visa before they enter Mexico or requiring them to seek asylum once they do enter. While the Mexican government would pay a political price and upset its southern neighbors, it might do so for the sake of good relations with the U.S., as it has done in allowing U.S. drug agents to operate in Mexico. But at present such a sacrifice would be political suicide given the acrimony Mr. Trump has stirred up over trade and immigration.

Similarly, the U.S. may never have needed tariffs to curb Chinese trade abuses had it first allied with other advanced economies -- as in 2014 when the U.S., Japan and European Union forced China to resume exports of industry-critical rare earths. Instead, Japan, wary of U.S. protectionism, is now nurturing warmer trade relations with Beijing.

Then there is the risk that U.S. policies actually trigger a new crisis. Tariffs and non-tariff barriers, such as invasive customs inspections, could disrupt the delicate supply chains that link the U.S., Chinese and world economies, a man-made version of the Icelandic volcano in 2010 or Thai floods in 2011 that disrupted global travel and manufacturing.

Meanwhile the U.S. tax cut and the borrowing that finances it are pushing upgrowth, interest rates and the dollar, sucking capital out of emerging economies from Brazil to Turkey. Capital may also flee China on expectations the yuan will be devalued to counter U.S. tariffs. Commodity and **oil prices** are already softening as a result, which could ricochet into U.S. shale oil investment.

That this hasn't hurt much yet is in great part because the Federal Reserve has been so restrained in raising interest rates. Indeed central banks world-wide remain bastions of technocratic competence and global cooperation.

But central banks can only do so much. Military and economic crises typically require many countries to act together in their collective interest as a way of advancing their individual interests. The U.S. used to lead such efforts. In the future, that isn't so sure.

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Markets

Deng's Take: Hopes Dim for a China Deleveraging; An escalating trade fight with the U.S. threatens to knock a few decimal points from China's economic growth

By Chao Deng
511 words
21 June 2018
06:37 AM
WSJ Pro Financial Regulation
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English

Beijing's two-year campaign to get a grip on the nation's runaway debt problem has its days numbered.

The Chinese economy is facing headwinds, as shown by ebbing indicators from business activity to household consumption. An escalating trade fight with the U.S. threatens to knock a few decimal points from China's economic growth, targeted at around 6.5% this year.

Analysts say the dual pressures mean Beijing could soon ease monetary policy. "You don't want two negative shocks compounding each other," said Zhiwei Zhang, chief China economist at Deutsche Bank. "That would be damaging."

China has made strides in reining in shadow credit. Annualized growth in total social financing, a measure of credit and liquidity in the economy, eased to an all-time low in May, with contractions in everything from trust loans to corporate bonds. The only form of credit still expanding was traditional bank loans.

But hitting growth targets remains Beijing's ultimate priority. As the prospect of punitive tariffs by the Trump administration becomes a reality, economists expect policy makers to ease efforts to control debt.

"It's necessary and likely," said Ning Zhang, an economist with UBS. Like many analysts, Mr. Zhang expects China to soon cut the amount of reserves banks have to keep with the central bank. That would potentially free up billions of yuan for banks to lend, making life slightly easier for Chinese borrowers.

Fueling expectations for such a move, China's State Council said late Wednesday that a targeted cut in banks' reserve requirement ratio was one of several measures it had identified to ease financing difficulties for small and micro firms.

Another option for Beijing is to ease restrictions on projects that encouraged local governments to invest in building roads and other infrastructure. A notable slowdown in infrastructure investment this year has added to worries about a weakening economy.

Within the financial system, regulators could go for a subtler easing move: softening the implementation of a far-reaching regulatory framework aimed at reining in risky lending by banks. The central bank and other financial regulators formally adopted the asset-management plan this April but have yet to roll out details.

There are indications that Chinese policy makers are moving in the direction of easing already. The central bank injected an unusually large amount of 200 billion yuan ($31 billion) in one-year funds into the banking system Tuesday. The measure was aimed at calming a jittery **financial market** on the back of U.S. tariff threats.

"They need to reserve tools for the rainy days," said Ting Lu, chief China economist at Nomura International (Hong Kong). The chance of easing climbs as the U.S. targets an increasing amount of Chinese goods, he explained. "The framework this year is very hard for China."

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WSJ PRO CENTRAL BANKING

Economy

Powell: Economy Supports Further Rate Increases | Central Bankers Warn on Trade Conflicts | BOJ: Downside Risks on Prices | Timiraos's Take: ‘Dots' Could Carry More Weight; The Wall Street Journal's central banking newsletter for Thursday, June 21, 2018

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Timiraos's Take: As Forward Guidance Fades, the ‘Dots' Could Carry More Weight

Powell Says Solid Economy Supports Further Fed Rate Increases

Central Bank Leaders Warn Trade Conflicts Could Damage Global Economy

BOJ Funo Says Attention Needed on Downside Risks on Prices

As Forward Guidance Fades, the ‘Dots' Could Carry More Weight

Federal Reserve Chairman Jerome Powell has a communications challenge.

He wants the Fed to provide less verbal guidance about its future plans now that policy is returning to normal. But he has also cautioned investors against reading too much into the Summary of Economic Projections—officials' estimates of future interest rates and other economic benchmarks—released quarterly.

The problem: Providing less forward guidance could perversely amplify markets' focus on the SEP, including the so-called dot plot, since nobody is talking about getting rid of those.

Mr. Powell repeated Wednesday his view that statements about the future path of interest rates were an important tool for the Fed after the financial crisis but were less useful now.

The Fed made greater use of the tool earlier this decade to convince markets it would hold rates very low for a long time.

Providing such forward guidance is both less useful and more difficult with rates rising to less stimulative levels.

Fed officials moved toward dialing back such guidance when they shortened their postmeeting statement last week. They dropped language that for years had implied rates would remain historically low.

Too much guidance risks "under-communicating" about inherent uncertainty in the economy, Mr. Powell said Wednesday. "That's a real risk for us—to say things and they're often taken as forecasts or even promises, and they're really not."

He has repeatedly said Fed officials' projections are neither a consensus forecast nor a commitment.

There is no elegant solution to this problem. Mr. Powell could keep hammering away at this message. He also could speak more often. His decision to hold a press conference after every meeting, instead of every other meeting, will go some distance toward that objective.

Once Mr. Powell has more company on the board, officials could explore other ways to clear up this dilemma.

For example, they could revisit discussions about compiling a consensus economic forecast. Most officials who participated in Federal Open Market Committee discussions in 2012, when officials considered and discarded the idea, have been replaced.

Until then, the Fed seems stuck with the dots—and the challenge of distancing itself from them at the same time that it is providing less forward guidance.

Key Developments Around the World

Powell Says Solid Economy Supports Further Fed Rate Increases

Federal Reserve Chairman Jerome Powell said sturdy U.S. economic growth has built a strong case for continuing to gradually lift interest rates, and he warned against policy complacency now that the central bank has nearly achieved its employment and price stability goals. "Today, with the economy strong and risks to the outlook balanced, the case for continued gradual increases in the federal-funds rate remains strong and broadly supported among" participants on the Fed's rate-setting committee, Mr. Powell said Wednesday. Mr. Powell spoke at the European Central Bank's annual policy conference in Sintra, Portugal, and his remarks highlighted the risks of allowing unemployment to fall too far below the level expected to prevail over the long run.

Central Bank Leaders Warn Trade Conflicts Could Damage Global Economy

Leaders of the world's top central banks warned Wednesday that escalating trade conflicts could ricochet through **financial markets** and hurt the world economy, potentially prolonging the era of ultralow interest rates. Rising tensions over trade come at an awkward time for major central banks, which have started moving away from easy-money policies introduced since the global financial crisis. In a moderated discussion in Portugal, the heads of the Federal Reserve, European Central Bank, Bank of Japan and Reserve Bank of Australia called for calm and warned that the costs of further escalation could be high.

Transcript: Powell, Draghi, Kuroda and Lowe Speak on Panel in Sintra

U.S. Federal Reserve Chairman Jerome Powell, European Central Bank President Mario Draghi, Bank of Japan Gov. Haruhiko Kuroda and Reserve Bank of Australia Gov. Philip Lowe discussed inflation, deflation, the Phillips curve, trade conflicts and other topics at an ECB conference in Sintra, Portugal. Here is a transcript.

BOJ Funo Says Attention Needed on Downside Risks on Prices

Bank of Japan policy board member Yukitoshi Funo said Thursday the bank should carefully monitor the downside risks for prices, and promised to continue the BOJ's current ultra-easy monetary policy. "Looking ahead, downside risks are large on prices, including medium- to long-term inflation expectations. It requires careful attention," Mr. Funo said in a speech.

SNB Stands Pat on Key Rate Despite Upbeat Economy

The Swiss National Bank on Thursday kept its key policy rate in deeply negative territory despite signs of healthy economic activity and slowly rising inflation, as the bank remains constrained by the actions of the European Central Bank. The SNB left its deposit rate at minus 0.75% as widely expected by economists, where it has been since January 2015. It also said the Swiss franc is "highly valued" and that it was willing to intervene in currency markets, if necessary, should the franc strengthen too much.

Brazil Central Bank Leaves Selic Rate Unchanged at 6.5%

Brazil's central bank held its benchmark interest rate steady Wednesday as a weaker currency hits the outlook for economic growth and inflation, while indicating it could leave rates unchanged at its next meeting. The bank kept its Selic lending rate at the historic low of 6.5%, where it has been since March, and said in the statement announcing the decision that "the balance of risks prescribes keeping the Selic rate at its current level," adding that the next steps depend on how indicators evolve until the next meeting, on Aug. 1.

Thai Central Bank Keeps Rates Steady

The Bank of Thailandleft interest rates unchanged Wednesday, as expected, opting to lend support to the economy amid global uncertainties as U.S.-China trade tensions intensify. The central bank's monetary policy committee kept its one-day repurchase rate at 1.50%. The Bank of Thailand has held the benchmark rate steady since a cut in April 2015. The decision was in line with a unanimous forecast of 11 economists polled by The Wall Street Journal. Most analysts expect the central bank to keep rates on hold this year. Five members of the monetary-policy committee voted to maintain the policy rate, while one official voted for a quarter-percentage-point increase.

Thursday

Time N/A

Bank of Mexico releases policy statement

7 a.m. EDT

Bank of England releases policy statement and minutes

8:45 a.m. EDT

ECB's Nouy speaks in Amsterdam

9 a.m. EDT

Minneapolis Fed's Kashkari speaks

4:15 p.m. EDT

Bank of England's Carney speaks

Friday

4 a.m. EDT

IHS Markit releases June composite Purchasing Managers Index for the eurozone

Why Has Economic Growth Slowed When Innovation Appears to Be Accelerating?

"Measured between quarters with identical unemployment rates, U.S. economic growth slowed by more than half from 3.2 percent per year during 1970-2006 to only 1.4 percent during 2006-16, and only half of this GDP growth slowdown is accounted for diminished productivity growth," Robert J. Gordon writes in a National Bureau of Economic Research working paper. He documents "the contribution to slower GDP growth of the separate components of demography—fertility, mortality, life expectancy, and immigration. Particular emphasis is placed on the interaction between rising inequality and the slower secular rise of life expectancy in the U.S. compared to other developed countries, both in the form of a large gap in life expectancy between rich and poor, and the stagnation of life expectancy for the lowest income quintile. Further contributions to slowing growth are made by a decline in the population share of both legal and illegal immigration and a turnaround from rising to declining labor force participation."

Smaller Banks Less Able to Withstand Flattening Yield Curve

"For the overall U.S. banking system, the effect on profitability of yield-curve flattening—the lowering of the difference between the yields of short and long-term debt—lasts about a year and is relatively small," write Pavel Kapinos and Alex Musatov in a Federal Reserve Bank of Dallas economic letter. "After the first year, the impact on large banks' profitability becomes positive; for smaller institutions, it stays negative and becomes larger. Recent yield-curve flattening is likely to more strongly affect smaller banks, reducing their profitability."

Flat Yield Curve Sends a Grim Message for Investors in 2019

Some "analysts and investors are worryingly eyeing the US yield curve, where the difference between the two and **10**-**year Treasury** yields has narrowed to just 37 basis points. That is the slimmest spread since September 2007. But interestingly, and worryingly, the global yield curve has now already inverted... Fortunately, the global curve inversion is largely a reflection of technical factors," Robin Wigglesworth writes for the Financial Times. "However, the global yield curve inverting should not be immediately dismissed as a technical fluke of no importance. The shape of the curve matters so much because it is the overall judgment of thousands and thousands of well-informed investors round the world, and the collective signal they are sending is that the outlook is far from rosy."

Sales of previously owned U.S. homes declined in May for the second consecutive month, signaling that a run-up in prices, rising mortgage rates and limited inventory may be holding down home purchases during the spring buying season.

Germany's leading auto makers have thrown their support behind the abolition of all import tariffs for cars between the European Union and the U.S. in an effort to find a peaceful solution to the brewing trade war.

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

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The New York Times

Business/Financial Desk; SECTB

New Fissures Over Output Are Dividing Oil Nations

By STANLEY REED
747 words
21 June 2018
The New York Times
NYTF
Late Edition - Final
2
English

VIENNA -- A meeting of major oil producers here in the Austrian capital has been dedicated to the theme of ''cooperation for a sustainable future.'' Soon after proceedings kicked off on Wednesday, though, the political tensions between them were laid bare.

For months, the world's main exporters of crude, including Iran, Iraq, Russia and Saudi Arabia, have worked together to curb their output to bolster **oil prices**. The uneasy coordination among several longtime rivals has helped sharply increase **oil prices** and slash what had been enormous supplies of unsold crude piling up in storage.

But faced with angry broadsides from President Trump, who is seeking cooperation from Saudi Arabia to force gasoline prices lower ahead of midterm elections in the United States, that cooperation now looks to be fraying.

At a conference arranged by the Organization of the Petroleum Exporting Countries grouping in Vienna, Iran's oil minister delivered blunt remarks arguing that it was Washington -- and not OPEC -- that was to blame for the high **oil prices** Mr. Trump has railed against.

''The real reason for the current **oil price** hike lies with the United States president himself,'' Bijan Zanganeh, the Iranian minister, said in a speech. Referring to American sanctions against Iran and Venezuela, Mr. Zanganah added, ''You cannot impose unilateral trade sanctions against two founding members of OPEC, two major oil producers, and at the same time expect the global market not to show adverse reaction.''

''The United States cannot expect OPEC to act against two of its founding members,'' he said. ''On the contrary, OPEC is independent, mature and reasonable.''

The Iranian minister's remarks appeared to be a pre-emptive shot at an emerging agreement between Saudi Arabia, OPEC's de facto leader but also Iran's main regional rival, and Russia, one of the world's largest producers, to increase oil output. The United States has put particular pressure on Riyadh, one of its main allies in the Middle East, to raise production.

Mr. Zanganeh's comments were just the latest indication that no matter how much OPEC officials talk about cooperation and stability, they are struggling to hold together a nearly two-year-old agreement to cap production. That deal has helped to more than double **oil prices** from their lows of early 2016 to around $75 a barrel now.

They preceded talks on Friday and Saturday here in Vienna in which OPEC members, as well as Russia and other major producers, will review the agreement. Failure to reach a deal to prolong the production caps could lead to a short-term fall in **oil prices**, but analysts say events in OPEC states -- like Libya, where fighting is threatening supplies, and Venezuela, where domestic turmoil has substantially curtailed production -- may outweigh any such shifts.

Moscow and Riyadh appear to want to keep the cooperation pact intact while also raising output, but that package may prove a difficult sell for other OPEC members. Any increases would most likely come from Saudi Arabia, while countries like Iran and Venezuela have little spare capacity. Those countries are in the difficult position of being able to benefit only from price increases.

For Iran in particular, production increases from Saudi Arabia would amount to rubbing salt in an already open wound. Not only are the two countries implacable foes, but Saudi Arabia -- as well as its Persian Gulf allies --

joined with Israel in lobbying the United States to withdraw from the 2015 agreement with Iran that checked Tehran's nuclear ambitions in exchange for the lifting of sanctions.

Sanctions that were reimposed by Washington in May are expected to lower Iran's production and exports, as refiners and traders across the world shy away from Iranian crude, while investors avoid the country's capital- and technology-starved oil industry. Iran could become a ''mini-Venezuela'' with precipitous output declines, Edward Morse, head of commodities research at Citigroup, said in an interview here.

Perhaps the biggest problem, though, is that the agreement to curb production has largely achieved its ends. Not only have prices risen but the oil glut that depressed prices in recent years has been reduced to more normal levels.

''Coming down a mountain, as every mountaineer knows, can be more perilous than climbing it,'' said Bhushan Bahree, an OPEC analyst at IHS Markit who was observing the Vienna meetings.

Follow Stanley Reed on Twitter: @stanleyreed12.

Bijan Zanganeh

Document NYTF000020180621ee6l00056

THE WALL STREET JOURNAL.
U.S. EDITION

Argentina To Rejoin MSCI Index

By Julie Wernau and Nicolas Parasie
423 words
21 June 2018
The Wall Street Journal
J
B10
English

MSCI Inc. returned Argentina to emerging-market status for the first time in nearly a decade, a move that is expected to provide a much-needed boost to the beleaguered country as it struggles to maintain credibility with investors after a widespread selloff in its currency.

Inclusion in the emerging-markets index is expected to draw billions of dollars in passive investment into Argentina's **stock market** at a time of vulnerability. The MSCI Argentina index is down 37% this year, the peso has fallen 33% against the dollar and Argentine bonds have dropped 14%.

Separately, MSCI said it would add Saudi Arabia to the emerging-markets index, a move that could attract tens of billions of dollars in foreign investment to the **stock market**. It also provides a vote of confidence for the Saudi **stock market** as the government considers taking public the giant state-owned oil company known as Aramco.

Both countries will officially join the emerging-markets gauge in May 2019, MSCI said Wednesday. Only foreign listings of Argentine companies will be included initially. Argentina had been classified as a frontier index and Saudi Arabia was a stand-alone index.

Morgan Stanley estimates the MSCI move could boost Argentine share prices by 20% over the next four months, based on $4 billion in fresh inflows. If MSCI had excluded the country from its emerging-markets index, that would have triggered another 6% decline in the market, the bank said.

Ehsan Khoman, head of research for the Middle East at Bank of Tokyo-Mitsubishi, estimates that up to $40 billion of fresh foreign inflows would be channeled into Saudi Arabia's **stock market** in the next year.

Argentina still faces an uphill battle as it contends with higher interest rates in the U.S., a rising dollar and other market dynamics that could turn investors away from riskier assets. Some analysts say runaway inflation and high local interest rates could lead the country into a recession.

MSCI said investors' confidence in Argentina's ability to maintain accessibility to the country's **stock market** was a key factor in the decision. MSCI warned that it would review the reclassification were Argentine authorities to introduce market-accessibility restrictions, such as capital or foreign-exchange controls.

In 2017, MSCI delayed the upgrade based on investors' concerns that recently implemented market-accessibility improvements needed to remain in place for a longer time to be deemed irreversible.

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THE WALL STREET JOURNAL.
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Changes On Way For VIX Auction

By Gunjan Banerji
438 words
21 June 2018
The Wall Street Journal
J
B1
English

Cboe Global Markets Inc. is revamping a feature of one of its most lucrative products, futures on the Cboe **Volatility** Index, which have come under scrutiny because of manipulation allegations.

The exchange operator is making changes to a monthly auction that determines final prices of futures tied to the VIX, also known on Wall Street as the "fear gauge." The changes amount to tweaks to its architecture.

Cboe has already made some adjustments to the technology that underpins the monthly auction and is planning to implement other changes that require regulatory approval. The VIX measures investor anxiety by looking at the prices they are willing to pay for options tied to the **S&P 500 index**. Because the VIX tends to rise when stocks fall, and vice versa, its derivatives are popular among traders to hedge portfolios or bet on the future direction of market **volatility**.

The moves by Cboe come after allegations of manipulation that have plagued the monthly auction in 2018. Volumes on VIX futures and options dwindled after hitting records this year. Fears of regulatory scrutiny have swept trading desks as lawsuits emerged over Cboe's marquee VIX products. The allegations have weighed on the company's stock. Cboe's shares are down 16% this year, while rivals have posted gains.

Chicago-based Cboe informed trading firms about some of the alterations Tuesday. Some are designed to lure more participation to the monthly auction, which in particular has come under fire for being antiquated and prone to spitting out unusual results. Traders have pointed to some of these results as signs of suspicious activity.

The company recently completed a planned transition of monthly **S&P 500 index** options trading to a more electronic system. Though U.S. stock and options exchanges have largely switched to electronic models and floor-based activity has dwindled across the board, Cboe's **S&P 500** options trading pits are one of the few last lively ones in the industry.

More robust participation by traders can reduce irregularities with the final VIX futures prices, like the odd result in April that got traders across Wall Street wary.

The May auction went more smoothly after a planned technology transition in late April. More traders also participated in the May auction, said Cboe President Chris Concannon in an interview this month.

Another recent change boosts the number of times the exchange sends signals to traders pertaining to **S&P 500** options orders to encourage participation in the auction and responses to buy and sell orders.

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World News: Central Bankers Say Dispute Could Threaten the World Economy

By Tom Fairless
728 words
21 June 2018
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J
A7
English

SINTRA, Portugal -- Leaders of the world's top central banks warned that escalating trade conflicts could ricochet through **financial markets** and hurt the world economy, potentially prolonging the era of ultralow interest rates.

Rising tensions over trade come at an awkward time for major central banks, which have started moving away from easy-money policies introduced since the global financial crisis.

In a moderated discussion Wednesday in Portugal, the heads of the Federal Reserve, European Central Bank, Bank of Japan and Reserve Bank of Australia called for calm and warned that the costs of further escalation could be high.

Global stock markets sagged this week after President Donald Trump called for a fresh round of tariffs on $200 billion of Chinese goods, upping the ante after he previously approved tariffs on $50 billion of goods.

"It's very worrisome and again, I can't see any positive," said ECB President Mario Draghi, who was hosting the event, Europe's answer to the Fed's annual economic symposium in Jackson Hole, Wyo.

Mr. Draghi warned that disputes over trade have created "considerable uncertainty" for the 19-nation eurozone economy, which has slowed sharply in recent months.

The European Union said Wednesday it would impose tariffs on U.S. goods valued at around 2.8 billion euros ($3.2 billion) in response to American import tariffs on steel and aluminum. But the EU's move is unlikely to discourage the U.S. from a second round of tariffs, possibly targeted at European autos, which would hit exports valued at 0.3% of the EU's economic output, said Oliver Rakau, an economist with Oxford Economics in Frankfurt.

In a shift reflecting those concerns, Mr. Draghi warned Tuesday that the bank could delay plans announced only last week to phase out its 2.5 trillion euro bond-buying program and suggested the timing of a first interest-rate increase could be pushed back.

Jerome Powell, chairman of the Federal Reserve, warned in the discussion that changes in trade policy "could cause us to have to question the outlook." The Fedlast week raised short-term interest rates and signaled a quicker pace of interest-rate increases to keep the U.S. economy from overheating.

While the tensions haven't yet dented U.S. economic growth, Mr. Powell said businesses increasingly were expressing concerns to the Fed about how the conflict might affect their plans for investment and hiring.

For Japan, whose central bank maintained its aggressive stimulus policies last week to support a softening economy, the trade conflict is "a matter of great concern," said Bank of Japan Gov. Haruhiko Kuroda.

The indirect impact on Japan's economy could be "quite significant if the escalation between China and the U.S. continues," Mr. Kuroda said, because it could affect the Asian supply chain centered on countries like Japan and Taiwan and across southeast Asia.

While the tariffs themselves might not derail the global economic recovery, the fallout could be magnified by investors through **financial markets**,said Australia's central-bank governor, Philip Lowe. "I believe what is happening [on trade] is incredibly worrying," Mr. Lowe said.

He added that "it wouldn't take that much for **financial markets** to turn this into a very big global event."

The problem for central banks, in Japan and elsewhere, is that they appear to have little ammunition left to deal with any new economic downturn after years of aggressive stimulus.

The value of assets held by the Bank of Japan is set to exceed the nation's annual economic output over the coming months, while the ECB's balance sheet also will continue to grow through the end of this year. Both central banks are still holding short-term interest rates below zero.

Few Tools Remain

To Fight Recession

Fed Chairman Jerome Powell said at the meeting in Portugal that central banks would have less capacity to fight any new recession because interest rates are already close to zero. The U.S. government also has less scope to increase spending than in the past, he said.

Bank of Japan Gov. Haruhiko Kuroda said he hoped "this escalation could be rescinded and a normal trading relationship between the U.S. and China would prevail."

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THE WALL STREET JOURNAL.

Markets

Why a U.S.-China Trade War Could Pay Off Down Under; Asian markets were mixed on Thursday, but Australian stocks are soaring

By Saumya Vaishampayan
538 words
21 June 2018
12:37 AM
The Wall Street Journal Online
WSJO
English

Asian stocks were mixed on Thursday, though many of the region's moves were muted. Japan's Nikkei 225 index rose 0.8%, while Hong Kong's Hang Seng Index lost 0.3%.

Thursday's Big Theme

Two of Australia's biggest trading partners are embroiled in a trade dispute. So why is the country's **stock market** on a tear?

What's Happening

Australia's S&P/ASX 200 has surged to its highest level in more than a decade. The index rallied 1.1% on Thursday, beating its regional peers. For the year, Australia's market is up 2.9%.

The timing of the rally's latest leg is curious.

Australian stocks took off late last week. That is around the time trade tensions between the U.S. and China re-escalated, sending stocks in many other countries tumbling.

But the S&P/ASX 200 has advanced 2.4% since Friday's close, making it the week's best performing major global **stock market**, according to FactSet. By comparison, the **Dow Jones Industrial Average** has dropped 1.7% this week, Germany's DAX has lost 2.4% and Hong Kong's Hang Seng is down 2.6%.

So what's going on?

There is an element of catch-up at play: Australian stocks are at their highest since January 2008, but they're still well below record levels. The country's **stock market** lagged behind many of its global peers last year, as a number of them hit all-time highs.

Prices for Australia's key export—iron ore—also haven't been hit by trade fears as much as other commodities. Iron ore futures in China have fallen 2.8% this week, less than the 5.7% decline in copper futures in London, according to Futuresource.

And the Australian dollar has slumped more than 5% against the greenback this year. That should give some relief to the Australian economy, which bodes well for the country's corporate earnings.

Market Reaction

"There's a growing view that Australia might actually benefit from a trade war," said Michael McCarthy, chief market strategist at CMC Markets in Australia.

Given Australia's established trade relationships with both Washington and Beijing, any attempt by either country to diversify from the other could end up boosting demand for Australian goods. China, for example, could look to buy soybeans from Australia instead of the U.S., he said.

Another boon for Australia comes from China's attempts to clean up its air. China has in recent years shifted to higher-quality iron ore, leading to less smog from steel production. Australia specializes in exporting the high-grade iron ore that China wants, said Robert Rennie, head of **financial market** strategy at Westpac.

"A trade dispute in the first instance doesn't change that," he added.

Elsewhere

The dollar briefly rose above 6.5 yuan in the offshore market on Thursday morning in Asia. That hasn't happened since January.

Lucy Craymer contributed to this article.

Write to Saumya Vaishampayan at saumya.vaishampayan@wsj.com

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THE WALL STREET JOURNAL.

Politics

White House Is Confident It Has an Edge Over China in Trade Dispute; Behind new tariff threats is a belief the U.S. has the upper hand in talks, administration officials say

By Bob Davis and Lingling Wei
1,533 words
19 June 2018
09:53 PM
The Wall Street Journal Online
WSJO
English

President Donald Trump 's escalation of trade threats against China reflects his belief that Washington increasingly has the upper hand in the dispute, administration officials said, adding he is prepared to withstand pressure from U.S. businesses that might suffer from the conflict.

Mr. Trump caught Chinese officials off guard with his announcement Monday evening about potential new tariffs. Should China retaliate against U.S. trade policies, the White House said, the U.S. would apply tariffs of 10% on as much as $400 billion in Chinese imports. China had earlier threatened to retaliate against the U.S.'s initial round of 25% tariffs on $50 billion on imports announced last week. The bulk of those tariffs go into effect July 6.

News of the new tariffs and the prospect of a trade war

roiled global markets Tuesday . The **Dow Jones Industrial Average** fell 1.1% and the Shanghai Composite Index dropped 3.8% to its lowest level since mid-2016. Indexes in major exporters Germany and France slid more than 1%. Commodities prices also took a hit, with soybean prices dropping 2.2% to their lowest level in more than two years.

The White House's tough stance represents the ascendancy, for now, of trade hawks in the administration, particularly White House senior trade adviser Peter Navarro and U.S. trade representative Robert Lighthizer . Both officials argue China represents a fundamental threat to the U.S. that needs to be countered, even at the cost of pain to the U.S. economy.

"It's clear that China has much more to lose" than the U.S. from a trade fight, said Mr. Navarro.

Mr. Lighthizer said additional tariffs wouldn't be imposed until the U.S. picked the products, and received industry comment, a process that will take months and leaves open the possibility of additional negotiations. But so far there is no indication that such talks are on the horizon, and the Trump administration is signaling that it is increasingly confident of achieving goals through a dramatically more confrontational approach to China.

Although Chinese government officials pledged to fight back forcefully, they didn't give any details of what they might do, as they have in the past. Beijing has threatened to match the initial U.S. tariffs dollar-for-dollar and impose them on the same day as the U.S. acts.

Next up from the administration is a plan to halt Chinese investment in U.S. technology, due to be released by the Treasury Department by June 30. Under the plan, which is still being developed, the U.S. would use a law designed to address national emergencies to block Beijing from acquiring what the White House calls "industrially significant technology." Export controls on such technologies would also be tightened, say administration officials.

Mr. Trump has backed away from threats before, and sided with advisers who take a less confrontational attitude toward China, including Treasury Secretary Steven Mnuchin . In April, Mr. Trump threatened a dramatic increase in tariffs on Chinese goods, but didn't follow through. Instead, he approved negotiations Mr. Mnuchin led to get China to buy more U.S. goods and make changes to its tariffs and other trade barriers. That led to a temporary reprieve in the tensions as the two sides sought to negotiate a truce.

The White House has since judged those efforts a failure, especially after Mr. Mnuchin and Mr. Trump were criticized by cable TV hosts and some lawmakers of being weak on China. During a June trade mission to China by Commerce Secretary Wilbur Ross , Beijing offered to buy nearly $70 billion in U.S. farm, manufacturing and energy products if the Trump administration abandoned tariff threats. Mr. Trump rejected that offer as another empty promise.

"The other side may have underestimated" if they thought the White House could be swayed by pledges of purchases, said Mr. Navarro. "That was a miscalculation."

The hard-liners in the Trump administration increasingly believe Beijing is vulnerable on trade because China exports far more merchandise to the U.S.—$505.5 billion last year—than the U.S. sends to China. In 2017, the U.S. exported goods worth $129.9 billion to China. Mr. Navarro said the U.S. goal is "enforceable, accountable, systematic change" in Chinese economic and trading practices.

Although global trade now accounts for less than one-third of China's gross domestic product, compared with nearly two-thirds in 2006, strong exports were a big reason why China's growth exceeded the government's target last year. A sharp slump in exports in the coming months, economists say, could threaten growth just as investments in Chinese factories and other fixed assets are slowing to multiyear lows, while Chinese household consumption is starting to weaken.

U.S. officials also note another vulnerability of their Chinese counterparts: While China imports less than the U.S., its economic growth is more dependent on what it does import, especially on the machinery and technology.

China has plenty of weapons it can employ to respond to the confrontational U.S. trade policies, including stepped-up regulations of American companies operating in China and stirred-up nationalist resentment.

In recent years, China has banned group travel to the Philippines, Japan and South Korea, during disputes with those nations, depriving them of revenue, according to officials in those countries. Beijing also has organized consumer boycotts and selectively increased inspections by regulators, say foreign companies in China.

At a closed-door meeting with a group of Chinese and U.S. economists and government advisers in late March, Lou Jiwei, China's former finance minister who now heads the country's national pension fund, said China won't be bullied into doing what the U.S. wanted the way Japan did in its trade dispute with the U.S. in the late 1980s and early 1990s.

China isn't the U.S.'s "mistress," Mr. Lou told the group, according to people familiar with the meeting. "China and the U.S. are like a married couple," he said.

The White House says it is protecting U.S. technology, which Mr. Navarro and others describe as America's "crown jewels," from Chinese predation. Beijing obtains U.S. technology by stealing it, the White House alleges, and by forcing U.S. companies in China to transfer technology to Chinese firms.

Tariffs are the first line of defense. Administration officials say the new tariffs will change incentives for foreign firms and prompt them to move manufacturing operations from China. Even if they relocate elsewhere in Asia rather than the U.S., that's a plus, the officials argue, because it will hinder China's ability to acquire advanced technology.

Josh Kallmer, senior vice president at the Information Technology Industry Council , a trade association of high-technology firms, says the administration's plans would hurt U.S. companies by driving up costs and making them uncompetitive.

The Trump administration's threatened tariffs "are not just counterproductive, they are irresponsible," he said. "You can't just pick up a factory and move it to Vietnam. It takes years to move physical operations. It takes months to renegotiate contracts. It's not a practical solution."

Administration officials counter that U.S. firms adapt more quickly than they acknowledge. They also argue that reducing Chinese influence over U.S. companies is worth the short-term pain. If U.S. companies are eventually able to operate in China without fear of government pressure, "this economy will be stronger, the global economy will be stronger," said Mr. Navarro.

On trade issues, U.S. big business has little sway among hardliners in the White House, who believe American corporations have been too quick to outsource jobs. Recognizing that, corporate lobbyists are working with consumer and farm groups, which are influential in coming midterm congressional races.

Additional tariffs on Chinese goods are bound to hit consumer products, they say, which could spark a backlash. Beijing has threatened to focus retaliatory tariffs on U.S. farm goods, hoping to produce a similar reaction.

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

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THE WALL STREET JOURNAL.
U.S. EDITION

REVIEW & OUTLOOK (Editorial)
The GOP's Trade Abdication

517 words
20 June 2018
The Wall Street Journal
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English

Would Republicans in Congress stay mute if a President imposed income or sales taxes on U.S. industries on an arbitrary whim? We doubt it, so it's dispiriting to see Senate Republicans let Donald Trump impose tens of billions of dollars in border taxes without so much as a vote of protest.

That's the sad story as GOP Senators last week blocked a vote on Bob Corker's amendment to reclaim at least some of the power to impose tariffs that Congress has ceded to Presidents. Perhaps Mr. Trump took the silence as assent because he is escalating. On Monday he threatened tariffs on up to $450 billion in Chinese goods, and **financial markets** are finally losing their foolish complacency. Shares in exporters vulnerable to retaliation like Boeing and Caterpillar fell more than 3.6% Tuesday.

Mr. Corker's bipartisan measure would have required Congress to approve trade restrictions that Mr. Trump is imposing under Section 232 of the Trade Expansion Act of 1962. This is the law that lets a President impose more or less whatever tariffs he wants with an elastic definition of national security. Mr. Trump has used this open-ended authority to inflict his 25% tariff on steel and 10% on aluminum, and he's threatening a 25% levy on imported cars under the same law. His new China tariffs are based on a different legal rationale (Section 301).

"I would bet that 95 percent of the people on this side of the aisle support intellectually this amendment," Mr. Corker said on the floor with some acidity. "And a lot of them would vote for it if it came to a vote. But, no, no, no. 'Gosh, we might poke the bear' is the language I've been hearing in the hallways."

Mr. Corker is right that GOP leaders fear a Trump tweet in the middle of election season. Some of them are also griping in private that Mr. Corker has the luxury of bucking the President because he isn't running for re-election. But Mr. Corker's modest bill isn't the political threat to Republicans. The growing damage from Mr. Trump's trade war is.

By not allowing trade votes, Republicans are giving Mr. Trump free rein to impose tariffs that are doing substantial economic harm to many of their constituents. Farm state Senators deserve a chance to vote against tariffs that are spurring retaliation against U.S. agricultural exports of everything from pork to apples. So do Senators who represent U.S. manufacturers. The fear of a Trump tantrum is precluding an important fight about what the party of free enterprise supposedly believes.

The economic fallout may also hurt the GOP's chances of holding the Senate in November. Democrats Heidi Heitkamp (North Dakota) and Claire McCaskill (Missouri) are running against the tariffs as a way to oppose Mr. Trump and defend their states' agricultural interests. The longer Republicans shrink from standing up to Mr. Trump's protectionism, the more voters will conclude that Republicans in Congress are complicit in the damage.

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The New York Times

Business Day; Energy & Environment
At OPEC Meeting, U.S. Pressure Frays Uneasy Agreement

By Stanley Reed
804 words
20 June 2018
01:02 PM
NYTimes.com Feed
NYTFEED
English

VIENNA — A meeting of major oil producers here in the Austrian capital has been dedicated to the theme of “cooperation for a sustainable future.” Soon after proceedings kicked off on Wednesday, though, the political tensions between them were laid bare.

For months, the world’s main exporters of crude, including Iran, Iraq, Russia and Saudi Arabia, have worked together to curb their output to bolster **oil prices**. The uneasy coordination among several longtime rivals has helped sharply increase **oil prices** and slash what had been enormous supplies of unsold crude piling up in storage.

But faced with angry broadsides from President Trump , who is seeking cooperation from Saudi Arabia to force gasoline prices lower ahead of midterm elections in the United States, that cooperation now looks to be fraying.

At a conference arranged by the Organization of the Petroleum Exporting Countries grouping in Vienna, Iran’s oil minister delivered blunt remarks arguing that it was Washington — and not OPEC — that was to blame for the high **oil prices** Mr. Trump has railed against.

“The real reason for the current **oil price** hike lies with the United States president himself,” Bijan Zanganeh , the Iranian minister, said in a speech. Referring to American sanctions against Iran and Venezuela, Mr. Zanganah added, “You cannot impose unilateral trade sanctions against two founding members of OPEC , two major oil producers, and at the same time expect the global market not to show adverse reaction.”

“The United States cannot expect OPEC to act against two of its founding members,” he said. “On the contrary, OPEC is independent, mature and reasonable.”

The Iranian minister’s remarks appeared to be a pre-emptive shot at an emerging agreement between Saudi Arabia, OPEC ’s de facto leader but also Iran’s main regional rival, and Russia, one of the world’s largest producers, to increase oil output. The United States has put particular pressure on Riyadh, one of its main allies in the Middle East, to raise production.

Mr. Zanganeh’s comments were just the latest indication that no matter how much OPEC officials talk about cooperation and stability, they are struggling to hold together a nearly two-year-old agreement to cap production. That deal has helped to more than double **oil prices** from their lows of early 2016 to around $75 a barrel now.

They preceded talks on Friday and Saturday here in Vienna in which OPEC members, as well as Russia and other major producers, will review the agreement. Failure to reach a deal to prolong the production caps could lead to a short-term fall in **oil prices**, but analysts say events in OPEC states — like Libya, where fighting is threatening supplies, and Venezuela, where domestic turmoil has substantially curtailed production — may outweigh any such shifts.

Moscow and Riyadh appear to want to keep the cooperation pact intact while also raising output, but that package may prove a difficult sell for other OPEC members. Any increases would most likely come from Saudi Arabia, while countries like Iran and Venezuela have little spare capacity. Those countries are in the difficult position of being able to benefit only from price increases.

For Iran in particular, production increases from Saudi Arabia would amount to rubbing salt in an already open wound. Not only are the two countries implacable foes, but Saudi Arabia — as well as its Persian Gulf allies —

joined with Israel in lobbying the United States to withdraw from the 2015 agreement with Iran that checked Tehran's nuclear ambitions in exchange for the lifting of sanctions.

Sanctions that were reimposed by Washington in May are expected to lower Iran's production and exports , as refiners and traders across the world shy away from Iranian crude, while investors avoid the country's capital- and technology-starved oil industry. Iran could become a "mini-Venezuela" with precipitous output declines, Edward Morse, head of commodities research at Citigroup , said in an interview here.

Perhaps the biggest problem, though, is that the agreement to curb production has largely achieved its ends. Not only have prices risen but the oil glut that depressed prices in recent years has been reduced to more normal levels.

"Coming down a mountain, as every mountaineer knows, can be more perilous than climbing it," said Bhushan Bahree, an OPEC analyst at IHS Markit who was observing the Vienna meetings.

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Bijan Zanganeh, the Iranian minister, delivered blunt remarks at a meeting of major oil producers. | Stefan Wermuth/Bloomberg

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THE WALL STREET JOURNAL.

Markets

What About Amazon? Dow Industrials Dumping GE for Walgreens Reflects Index's Dilemma; A price-weighted methodology complicates the index's adaptation to a 21st-century economy

By Michael Wursthorn and Akane Otani
1,007 words
20 June 2018
06:24 PM
The Wall Street Journal Online
WSJO
English

The **Dow Jones Industrial Average** has ejected numerous blue-chip industrial companies over the past decade, including miner Alcoa Inc., Westinghouse Electric Corp. and this week General Electric Co., in an effort to adapt a 19th-century index to a 21st-century economy.

That path has become increasingly fraught, in part because of the limitations of how the index is constructed.

Critics also contend the index's selection committee has been removing troubled companies to avoid undermining the average's long-term performance.

"Honestly, I didn't like the move," Robert Pavlik, senior portfolio manager and chief investment strategist at SlateStone Wealth, said of the decision to drop GE. "It's supposed to be an industrial average that is reflective of the overall economy of the United States, and if that's the case, then why replace it with a Walgreens?"

Component stocks of the Dow are selected by the index committee, a group that includes editors of The Wall Street Journal, which is published by Dow Jones & Co., a part of News Corp.

Previous component swaps in the index tended to highlight a particular company that had disrupted entire industries and reshaped consumer behavior, like Visa Inc. and Microsoft Corp., or sought to maintain a balance with a like-for-like replacement.

In 2015, AT&T Inc. was replaced with Apple Inc., which had upended the technology and communications industries with its iPhone and other mobile devices. Two years before that, the index committee removed Bank of America Corp., which was still struggling under the weight of the 2008 financial crisis, for a healthier Goldman Sachs Group Inc., while Alcoa was replaced with then-athletic apparel powerhouse Nike Inc.

The addition of Walgreens, however, has puzzled some investors. The large retailer is part of the consumer-staple sector of the **stock market**, which has struggled under the shadow of Amazon.com Inc.'s e-commerce prowess.

"When you think about the direction the economy is going in, and even the names that dominate the market today, you're not looking at a drugstore retailer who very much itself could come under threat from Amazon," said Michael O'Rourke, chief market strategist at JonesTrading. "If you want to be representative of the economy and where the economy is going, you gotta add them."

But its omission reflects the constraints of the Dow's methodology.

Since the index's creation by Charles Dow, founding editor of the Journal, the average has been price weighted, meaning the bigger the **stock price**, the larger the sway for a particular component, and vice versa. So Boeing, which is trading at $342.69 a share, carries about 27 times more influence than GE at around $12.88 a share. That is different from indexes such as the **S&P 500**, which are weighted by components' market capitalizations.

Although GE fell 45% last year, it barely made a dent in the index. Caterpillar, meanwhile, has been one of the top stocks to help yank the index higher despite having a market cap smaller than the troubled conglomerate.

Amazon's **stock price**, currently about $1,750 a share, would cause massive day-to-day gyrations in the Dow. If the company were in the Dow on Wednesday, its less than 1% rise would have contributed roughly 105 points to the Dow, which fell just 42 points during the session.

With Walgreens, consumer-staple stocks have four representatives in the Dow, the same number of consumer-discretionary stocks, financial firms, health-care companies and industrial companies once GE was removed—a more equal footing across sector lines than in the **S&P 500**, which gives its heaviest weightings to industrial, tech and financial companies.

Given the uncertain future of the sector, Walgreens could follow the path of other Dow components that entered and left the index in fairly brief fashion due to their shrinking size or turbulence within the companies. Kraft Foods spent about four years in the index before it was removed in 2012 after the spin off of its North American grocery business, in favor of UnitedHealth. Bank of America got five years.

The removal of troubled businesses appears to have helped keep the index moving higher. The indexing committee made changes to the Dow over eight separate years since 1998, and the index ended up posting positive returns in six of those years.

Not all investors think GE's removal from the index cements its status as an underperforming stock. In fact, S&P Dow Jones Indices' latest decision has some investors feeling more optimistic now about GE's odds of rebounding.

Going back to 1972, stocks that have been removed from the Dow industrials have tended to outperform it over time, with companies outpacing the blue-chip index by an average of 9.2% over the following 12 months, according to an analysis by Ned Davis Research.

To some investors and analysts, the trend suggests that the index committee behind the Dow industrials has often mistimed its decisions, removing a company before it has fully had a chance to make a turnaround.

Analysts are predicting GE shares will rise over the short term, with the mean price target for the stock clocking in at $16.42, according to FactSet, 27% above their current price.

"It's certainly going to be a name that's on my radar," Mr. Pavlik said. "When they kick it out of the Dow, I think it highlights that it's probably near its bottom."

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THE WALL STREET JOURNAL.

Markets

Investors Worry About China Devaluing the Yuan, but the Currency is Rising; One gauge of the currency's strength indicates no efforts to devalue this year

By Mike Bird
490 words
20 June 2018
04:44 AM
The Wall Street Journal Online
WSJO
English

The prospect that China would use currency devaluation to retaliate against any escalations of U.S. tariffs loomed in the aftermath of a sharp drop in the country's stock markets.

But one gauge of the Chinese currency's strength indicates no efforts to devalue this year.

On Wednesday, the central bank set its reference rate for the yuan at 6.4586 to the dollar, 0.5% weaker than Tuesday's rate and the lowest since January.

"One would imagine that China will be thinking about currency devaluation again," said Rabobank senior Asia-Pacific strategist Michael Every in a research note. The yuan doesn't trade freely, and analysts are often left wondering what the People's Bank of China has in mind for the currency. Devaluation is one of Beijing's most powerful economic tools.

China imports far less from the U.S. than it exports to it and could use depreciation as an alternative way to retaliate against tariff increases.

Though the U.S. dollar has risen 2% against the yuan this year, the trade-weighted measure of the yuan published by the PBOC, the CFETS index, has risen since trade tremors began with the announcement of U.S. steel and aluminum tariffs in March.

The yuan is higher this year against the euro, yen, British pound, Australian dollar and Korean won. Though the dollar exchange rate is most commonly referenced, those currencies make up around 46% of the basket used to calculate the index, versus the greenback's 22% weighting.

The CFETS index hit a two-year high in May and was a fraction below that level on June 15, the last weekly fix for the trade-weighted measure.

The lack of any broad depreciation in the yuan suggests that China isn't attempting to gain an unfair advantage over its trading partners in the foreign-exchange market.

That isn't a recent phenomenon. The Bank for International Settlements tracks countries' real exchange rates, adjusted for inflation. It shows the yuan has risen around 90% against 61 international currencies since its series began in 1994.

Recall what happened the last time China cut the yuan's value: A rapid weakening in 2015 sparked capital outflows as investors attempted to remove money from the country and avoid further depreciation. The government responded by crimping the ability to move money out of China.

Devaluing again could damage Beijing's long-term goal to open its **financial markets** and promote the yuan as an international currency, according to Bilal Hafeez, a strategist at Nomura.

Write to Mike Bird at Mike.Bird@wsj.com

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THE WALL STREET JOURNAL.

U.S. Markets
Markets
S&P 500 Gains After Trade Selloff; Many investors still expect the U.S. and China will dial down their tariff plans

By Riva Gold and Amrith Ramkumar
697 words
20 June 2018
05:13 PM
The Wall Street Journal Online
WSJO
English

* Stocks stabilize following Tuesday drop

* Treasury yields rise

* Walgreens, 21st Century Fox among best performers

U.S. stocks stabilized a day after trade tensions rattled markets around the world.

The S&P 500 ended a three-session streak of declines, buoyed by gains in shares of real-estate firms, and the tech-heavy Nasdaq Composite closed at a fresh record.

Investors this week have been more seriously considering the chance that the world's two largest economies could embark on a growth-hindering trade war, but many still expect the two countries to ultimately dial down their plans and reach a compromise. Some investors have been encouraged that large companies continue to oppose protectionist trade policies that could hurt their global businesses.

"Our base case is this gets walked back…but it's getting more serious now," said Tim Courtney, chief investment officer at Exencial Wealth Advisors. "The longer it goes on and the further we go down this path, the greater the chances are that this could actually stick."

The S&P 500 added 4.73 points, or 0.2%, to 2767.32. The Nasdaq rose 55.93 points, or 0.7%, to 7781.51. The Dow Jones Industrial Average closed down 42.41 points, or 0.2%, at 24657.80 in a seventh straight session of losses—its longest such streak since March 2017.

Wednesday's moves came as analysts weighed news that Germany's leading auto makers have thrown their support behind the abolition of all import tariffs for cars between the European Union and the U.S. The move comes after President Donald Trump late Monday called for his administration to identify $200 billion in Chinese goods for a fresh round of tariffs.

Despite recent trade fears and anxiety about higher interest rates, some investors think steady earnings growth will boost stocks moving forward.

"I'm not too worried," said Chris Bertelsen, chief investment officer of Aviance Capital Management. "If it turns out to be the great trade wars of the 1930s, I will be wrong, but that's a position we're willing to take."

The yield on the benchmark 10-year U.S. Treasuryyield climbed to 2.928% from 2.893%. Yields rise as prices fall. Federal Reserve Chairman Jerome Powell said at the European Central Bank's annual policy conference Wednesday that sturdy U.S. economic growth has built a strong case for continuing to gradually lift interest rates.

Walgreens Boots Alliance was among the S&P 500's best performers, adding $3.39, or 5.2%, to $68.00 following news that it would be added to the Dow Jones Industrial Average, replacing General Electric.

Shares of 21st Century Fox rose 3.21, or 7.2%, to 47.50 after Fox and Walt Disney announced a new merger agreement, increasing the value of the deal and adding a cash component. Fox and Wall Street Journal owner News Corp share common ownership.

PayPal shares also climbed after the company agreed to acquire financial-technology company Hyperwallet Systems Inc. for about $400 million.

Among decliners, shares of Starbucks fell 5.21, or 9.1%, to 52.22 after it said it would close 150 U.S. stores in its 2019 fiscal year. Oracle was also an **S&P 500** laggard after it warned currency conversions would weaken the company's quarterly performance.

Elsewhere, the Stoxx Europe 600 added 0.3% to snap a three-session losing streak, with bank shares among the best performers.

Earlier, Japan's Nikkei Stock Average rose 1.2% and Hong Kong's Hang Seng advanced 0.8%, after both indexes tumbled on Tuesday.

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Markets

Cushman & Wakefield Files for IPO; The company could seek about $1 billion and seek a valuation in excess of $5 billion, according to people familiar with the deal

By Peter Grant and Maureen Farrell
758 words
20 June 2018
06:22 PM
WSJ Pro Private Equity
RSTPROPE
English

Real estate services firm Cushman & Wakefield filed preliminary plans for an initial public offering, hoping to cash in on the nine-year **bull market** in the commercial real-estate industry.

The company could seek to raise about $1 billion in the IPO and seek a valuation in excess of $5 billion, according to people familiar with the deal, though pricing of the deal can change until a company prices its IPO. A Cushman spokesman declined comment beyond the registration statement it filed with the Securities and Exchange Commission.

Cushman & Wakefield's owners, an investment group led by private-equity firm TPG, purchased the firm and several other commercial real estate businesses in 2014 and 2015 for more than $3.5 billion. The group's plan has been to build a global giant that would compete with CBRE Group Inc. and JLL. Cushman has about 400 offices in 70 countries, according to its SEC filing.

The commercial property brokerage business has been strong in recent years thanks to economic growth in many parts of the world that's fueled demand for office, retail and industrial space. Sales activity also has been high as investors have sought assets with higher yields than bonds and less **volatility** than stocks.

Cushman's revenue was $6.92 billion in 2017, up from $6.2 billion in 2016, the firm's filing said. By comparison, CBRE's revenue for 2017 was $14.2 billion and JLL's was $7.9 billion.

Analysts have long expected an initial public offering of Cushman by the ownership group, which also includes PAG Asia Capital and Ontario Teachers' Pension Plan. Private-equity firms like TPG often use IPOs as a way to exit or partially exit their investments.

Soon after acquiring Cushman in 2015, the owners hired industry veteran Brett White to be chief executive and merge the firm with other big operations they acquired including Chicago-based DTZ and Washington, D.C.-based Cassidy Turley.

Mr. White worked at CBRE for close to two decades, the last seven as chief executive, and played a major role in that firm's 2004 IPO. He stepped down from CBRE in 2012.

Once Mr. White joined Cushman, the race was on. There has been rampant speculation in the commercial property business over whether he would be able to combine the three firms and improve margins before the bull-run in the commercial real-estate market ended.

That window still appears to be open. CBRE's shares are trading in the $49 a share range, close to their record high. JLL's shares are approaching the record high they hit in 2015.

But the IPO market has been tricky lately for the commercial property industry. For example, in early December, Newmark Group Inc., whose chairman is Howard Lutnick of Cantor Fitzgerald LP fame, planned to sell 30 million shares at a price range of $19 to $22 a share.

But investor response was weak. The offer size was cut to 20 million shares and it priced at $14. Newmark shares were trading at $15.51, up 73 cents, Wednesday in 4 p.m. trading on **Nasdaq**.

Mr. White has been beefing up Cushman's revenue partly by recruiting top producers from other firms. For example, in 2016 he poached a team of high-profile sales brokers, led by Doug Harmon and Adam Spies, from Eastdil Secured LLC.

In the past four years, Cushman's margins have grown from 7% to 10% when computed using fee revenue and adjusted earnings before interest, taxes, depreciation and amortization, according to the firm's filing. By comparison, CBRE reported an 18% margin using a comparable calculation.

Also, Cushman has a high debt level compared with some of its peers, $3.07 billion as of March 31. The firm plans to use the IPO proceeds partly to pay down debt, the filing states.

Cushman & Wakefield was founded in New York in 1917. The firm moved its headquarters to Chicago, the home of DTZ, after being acquired by the TPG group. According to the filing the TPG group would retain voting control after the IPO.

Underwriters include a group of banks led by Morgan Stanley, J.P. Morgan, Goldman Sachs & Co. and UBS Investment Bank.

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WSJ PRO CENTRAL BANKING

Economy
Transcript: Powell, Draghi, Kuroda and Lowe Speak on Panel in Sintra; Central bank leaders discuss inflation, the Phillips curve and trade conflicts at an ECB conference in Portugal

11,413 words
20 June 2018
05:41 PM
WSJ Pro Central Banking
RSTPROCB
English

Four of the world's top central bank chiefs spoke on a panel Wednesday, June 20, 2018, at a conference in Sintra, Portugal. They were U.S. Federal Reserve Chairman Jerome Powell, European Central Bank President Mario Draghi, Bank of Japan Gov. Haruhiko Kuroda and Reserve Bank of Australia Gov. Philip Lowe.

Stephanie Flanders, of Bloomberg Economics, moderated the exchange. They discussed inflation, deflation, the Phillips curve and other topics. Here is a transcript, edited for length and clarity.

STEPHANIE FLANDERS: Well, we've had some spirited debates in the last couple of days around price and wage setting in advanced economies. Do central bank talk too much to markets? Who killed the Phillips curve? I think the feeling was there were potential culprits in this room. Maybe we can have a polling question on who killed it.

But now we get to hear from a group of four individuals who collectively probably have more capacity to actually change price and wage setting in advanced economies than anybody else, maybe even more than (U.S. President) Donald Trump perhaps. (Laughter.)

We're going to have brief, I hope, relatively informal remarks from each of them at the beginning, I get to ask a few questions, and then I promise you will get to ask lots of erudite questions as well.

But President Draghi, do you want to kick us off?

MARIO DRAGHI: Well, thank you, Stephanie.

The first point is there is clearly a variety of reasons why the response of inflation and wages has been so slow, and they go from measurement of the slack, low productivity, the trade unions have disappeared, structural reforms, labor supply has gone up – it has increased a lot – and then non-wage-related aspects like people wanting more stability rather than higher wages, especially because their employment is of low quality, and then the importance of past inflation.

Now to disentangle all these reasons, it's very difficult. But one conclusion is that we see that all these – the combined effect of all these reasons is gradually washing out, is gradually waning.

A good example is one given by the importance of past low inflation for a long time. The ECB staff has calculated that low inflation – past low inflation has dragged about 0.2 percent out of wage growth in the last three years per year – 0.2 percent per year. And now we see that this effect is waning out, and as headline inflation is picking up, current headline inflation becomes more and more important, and past low inflation is losing importance. And so that, in a sense, also says that anchoring inflation expectations was crucial and remains crucial, and fortunately, they are well-anchored.

So once this is said, we see that nominal wages are indeed increasing no matter which measure we take. We take compensation per employee, we take compensation per hour, we take negotiated wages – all of them are going up, and they are going up around – now it's 1.9 percent, the last data point for the compensation per employee, and compensation per hour is the same – about the same thing.

Having said that, is this going to be translated into higher inflation? Well, here I think the record is a little more mixed. For example, we had – we had an increasing wage growth, by 0.8 percent, between 2016 and 2018, in this year, but the increasing inflation was only 0.1 percent, and because productivity had gone up by 0.7.

Now what do we expect for productivity? We do expect it will grow less than it has done in the late stage of the cycles, and wages – nominal wages will grow more than they have done in the – up to now.

So all in all, we see the union labor costs on an upward path, and by the way, the other consideration, which was touched in the previous discussion, was related to pricing power, the coming back of pricing power. And there, again, we see encouraging signs because, if we look at an index which more closely reflects input prices; namely the domestic price – domestic non-food price inflation, in April that has gone up by 0.5 percent, which is the highest rate since, I think, in the last six, seven years. So all in all, this is encouraging.

Now what about e-commerce? Is this going to dampen this process of recovering inflation? And again, the previous discussion about whether an increasing concentration does affect the rate of inflation, to some extent, gives some light on this issue. Now the answer that we have is that we find very little evidence that e-commerce has any effect on inflation. It clearly has increased price transparency, clear may have some compression of margins, some cost saving. But all in all, in the aggregate, this doesn't show into a permanent lower inflation. So probably the effects of the e-commerce and other aspects of globalization have to do more with the composition of industries rather than with an aggregate effect that we don't – we cannot find in the data – an aggregate, permanent effect.

So all this makes us confident that inflation is converging towards our objective, and we draw this confidence by the tighter – the ever-tight labor market, by the high-capacity utilization rates, by – and frankly by – as I will say in a moment, by the continuing ample monetary accommodation – also by the disappearance of what we call the tail race of deflation.

So all this leads us – has led the (ECB) governing council last week to give guidance on monetary policy, and the first thing is we need – as I said last week at the press conference, we need to make sure that the ample degree of accommodation that is currently incorporated into the financing conditions on which the staff projections are predicated is maintained for as long as necessary in order to bring about the convergence of inflation towards our objective.

And then we went through the various measures. We said that we intend to maintain our portfolio of accumulated securities for an extended period of time after the end of net purchases, and in any event as long as necessary.

And then we enhanced our guidance on future rate path for our key interest rates. We said that we expect to hold them at the present level at least through the summer of 2019, and in any case for as long as necessary to ensure that inflation evolves along a trajectory that is aligned with the sustained adjustment path that we expect to see in the medium term.

JEROME H. POWELL: (EDITOR'S NOTE: Mr. Powell at this point delivered prepared remarks that have been posted to the Fed's website: https://www.federalreserve.gov/newsevents/speech/powell20180620a.htm and so we won't transcribe them here. You can read The Wall Street Journal's story on the speech here. https://www.wsj.com/articles/powell-says-solid-economy-supports-further-fed-rate-increases-1529501509)

PHILIP LOWE: In some ways I am the odd one out here. I come from a small economy, not a larger one. We've had positive interest rates for the last decade. We haven't had to go anywhere near zero. We haven't done quantitative easing. We haven't embraced forward guidance. And we've had 27 years without a technical recession, and I'm hoping we can extend that a while longer. (Laughter.) As I said, odd one out.

But I don't really feel like the odd one out, though, because the issues we're discussing here in Sintra are really at the core of the issues we're discussing in Sydney. In Australia, the inflation rate has been below the midpoint of our target for some years. And it's going to stay that way, I think. Wage growth has repeatedly surprised on the downside. And the current rate of wage growth isn't consistent with us achieving our inflation target on a sustained basis. So, like others, we're grappling with why we find ourselves in this situation.

The fact that it's happening in so many countries suggests to me that there are global factors at work, and they are probably structural in nature. And the result of those factors is that the inflation process looks very different in many countries. And at the heart of that I think is the wage process, which looks different. Whether that's going to be permanent, that's hard to tell. But it's certainly persistent enough that it's important for policy. So what I'd like to do in my time is to offer some reflections on two issues that are really at the heart of this conference. And that is: Why is the wage process different? And how much of it's structural? And what are the policy implications of that?

So the wage process, as I said, is different. The relationship between wages and unemployment looks to have changed. And there are three sets of factors that I think are really important here. One is the changes in the industrial relations landscape. And we saw a really good example of that this morning in Professor Schonberg's paper. I think the evidence there is pretty compelling. Changes in industrial relations arrangements in Germany have affected wage and employment outcomes. And the Australian experience is very similar to the German one. It's hard to escape the conclusion that changes in industrial relations has changed the inflation process.

The second one – or, the second factor – I think this is actually more important – is that there's increased perceptions of competition arising out of globalization and technology. Everyone feels like there's more competition. And one of the first things you learn in economics is that if there's more competition prices aren't as high. We discussed this in the earlier session. And there are a couple of factors that are driving those extra perceptions of competition. One is globalization. There's hundreds of millions of extra people that have entered the global labor force, particularly in China and India.

And first of all, that affected manufacturing wages around the world and now I see it affecting services wages. Many more services sectors becoming tradable. I see a lot of examples where business services that used to be supplied in Sydney are now supplied in Manila, or Chengdu, or Bangalore. And that's meaning that everyone feels like there's more competition. And the other factor that's adding to the sense of competition is the nature of technological progress. It's much more likely being embedded in intellectual capital and physical capital. And we're also seeing widening gaps between the leading firms and the laggard firms. And both of those features are affecting the wage dynamics.

With technology progressing so quickly, and particularly for the leading firms, many firms having trouble keeping up. They're having trouble adopting the new technologies. And to remain competitive, they focus on what they can control, and that is their costs. And the main cost they can control is their labor costs. So the technology progress is leading, for many firms, to have a very, very strong mindset on controlling costs. Again, I see lots of examples of this in Australia. Almost every business meeting I go to, business people complain that it's incredibly hard to find workers.

And, I rather naively ask, well, why don't you pay more, attract some workers from another firm? And when I do that, they look at me as if I'm completely mad. That would be the last thing they would do. And I typically get a lecture about how competitive the world is. There's competition from China, Japan. And they worry about kind of technology. And they say, the last thing I can do is increase my costs. It's the one variable I can control. So there's a very strong mindset that I've got to control costs. And I think it's coming from competition. It's a global factor. And it's structural.

The third factor that's affecting the relationship between wages and unemployment is that labor supply in many countries is turning out to be much more flexible. And we're seeing this in a rise in the participation rate. There are a variety of reasons for this. One is – and we see this, again, in Australia – rising labor force participation by all the people as health outcomes have improved. We've seen big advances the health outcomes for many people. And where there's not – our bodies are lasting longer as we're working in services rather than manufacturing.

And that's allowing people to stay in the labor force longer, particularly when there are jobs there. I think that's quite an important factor, and the increasing acceptability of part-time employment is allowing many women in particular to stay in the labor force longer. So the labor supply is turning out to be quite flexible. So even though we're seeing very strong employment growth in a lot of countries, it's not translating into higher wages. So things look different, industrial relations, increased perceptions of competition, and increased labor supply. And I think those factors are going to be around for a long time. So I don't expect the situation that we're dealing with to change quickly.

So what are the policy implications of this? The main one, to me, is that the system that we're operating in looks less inflation-prone than it once was. And that's reflected in most of us worrying about inflation being too low, not too high. It's a very different world than when I was at university. So listening to the discussion of the past two days, I've been trying to think about – or trying to listen for ideas about how we deal with this world that is less inflation prone. And I can take the liberty of summarizing the things I've heard under three broad kinds of approaches one could adopt here. One is that central banks should just try harder. The basic conception of how the economy is working is fine, we just need lots of monetary stimulus. We need to keep at that. We need to just try harder. And eventually it will turn out OK.

The second perspective – a couple of people touched on this yesterday – is we just need to accept that inflation will be low for a while. After all, low inflation isn't that bad. Now, central banks want to achieve their inflation targets. That's clear. But most people out there in the communities that we're supposed to be serving don't really care that much if inflation's a big lower than the target, especially if the labor market outcomes are OK, if there are plenty of jobs being created. So the second perspective is, well, it's not – it's not kind of fantastic, but we just got to be patient, accept that inflation is going to be low for a while, and there's not really a great loss of social welfare from that.

The third perspective is one introduced by (inaudible) yesterday. He said, well, just lift inflation expectations. Central banks should embrace social media. They should communicate better, make it very clear what inflation expectations should be, and the problem is kind of solved.

I think you can make a case for each of those perspectives. I don't think there's a right answer. I see a few problems, though, with the "try harder" approach, just keep on solving this problem with monetary stimulus, is I don't see the risk/return tradeoff from that approach being particularly attractive. In terms of return, the effectiveness of monetary stimulus in driving up inflation, kind of I think there's a question mark over how effective that is. And I can see clear side effects. And the side effects come on the financial side.

If interest rates are low and the economy is growing quite well, that's a great environment to borrow, to buy assets. And we're seeing some of that. So we see higher debt and higher asset prices. It's helpful now, but eventually interest rates will hopefully need to correct, and some of those developments on the financial side will need to be reversed. And that's going to pose risk. So the effectiveness of more monetary stimulus to solve the lack of inflation is questionable, and I see clear risk from doing that.

So I think that does leave us with the possibility of accepting that inflation might be just a bit lower than we'd like for a while. That's difficult for central banks to accept, as they see their job to kind of deliver on the inflation target. But it's not so difficult to accept that if you see your job or your mandate as broader than just delivering on a specific rate of inflation. In Australia, our mandate was written back in 1959. And it hasn't changed since then. We haven't swung with the fashions in central banking. We don't have a single mandate. We don't even have a dual mandate. We have a triple mandate. (Laughter.)

That's price stability, full employment, and the general welfare of the Australian people. (Laughter.) That's an unfashionable mandate, perhaps, in this room, but I am really glad that we have that mandate, especially in the current environment. And I use all three elements of that mandate when I'm explaining what we're doing and why we're doing it. I often ask rhetorically in public and to the politicians: Do you think it would serve our collective welfare to have yet more monetary stimulus so that we can get back to inflation more quickly, if the main way we got back to inflation more quickly was encouraging people to borrow more and push up asset prices even further?

So not everyone's going to answer that question kind of the same way, but most people say, look, no, that's not worth it, especially if the labor market's generating sufficient jobs, which is certainly the case. Last year we've had 3 percent employment growth. So in our case, my view has been that the welfare-maximizing approach – which is really what we're about, maximizing the welfare of the people – is to be patient as long as the labor market is improving. As long as we're moving in the right direction, we don't need to force the process more quickly through monetary stimulus.

One thing, though, that we have done in an effort to get there a bit more quickly is a version of option three, lifting expectations, because as I said yesterday, it's lifting wage expectations. My concern has been that a 2 percent wage norm has become the standard in Australia, and we're getting reasonable labor productivity growth, so 2 percent wage growth and reasonable labor productivity growth doesn't make for 2 ½ percent inflation on a sustained basis.

So I've been talking publicly quite a lot about trying to lift wage norms back to start with a 3 rather than a 2. Whether that works or not, I don't know, but I'd rather do that than try and deliver more monetary stimulus to get inflation rise. I'd rather do it by trying to lift wage expectations.

MR. KURODA: Thank you. Japan's economy has improved significantly over the past five years since the introduction of quantitative and qualitative monetary easing – or QQE – in April 2013. The economy is no longer in deflation, which is defined as a sustained decline in prices. However, wages and prices have continued to show relatively weak development compared with a strong economic expansion.

The mechanism behind this phenomenon is not entirely clear. Today I would like to talk about the recent experience in Japan where the sluggishness in wages and prices seems to be more evident compared with other advanced economies, and discuss its implications for the Bank of Japan's monetary policy.

First is firms' wage-setting stance. For the past few years, total cash earnings per employee have been rising, albeit (with) fluctuations. However, their pace of increase has been moderate compared to the labor market tightening with the unemployment rate being at a record low level of 2.5 percent. In particular, base salaries of full-time employees, which account for almost 70 percent of total employee income, have not risen much despite general labor market tightening.

In Japan, lifetime employment has been widespread, and labor mobility across firms has been relatively low. Therefore, wages of full-time employees tend to reflect the labor market conditions insufficiently, at least in the short run.

In Japan, wage negotiations between labor and the management take place at major firms every spring where the rate of increase in base pay is decided. The rate has been almost zero percent since around 2000 under the prolonged deflation. In 2014, when actual prices started to rise, there was a return to base pay increase for the first time in nearly 15 years. However, the problem is that the pace of increase in base pay still lacks strength. On this point, some have argued that – reflecting that both labor and management in Japan place priority – high priority on the stability of employment and wages. Firms avoided the large-scale layoffs and wage cuts during the prolonged deflation so that firms cannot simply switch to increasing wages, even when the economy grows and the labor market conditions tighten. The deflationary mindset that has become entrenched among people has been quite tenacious, and it will take time to completely dispel this mindset.

Second is firms' price-setting stance. Even though moderate wage increases have been taking place, wage costs have not yet been directly passed on to prices of products and services. Firms that face increases in wage costs will generally consider the following two options to maintain the same level of profitability. One is to pass on the increased wage costs to sales prices, and the other is to improve productivity through streamlining of business processes and labor-saving investment. So far, many firms in Japan have been making effort to raise their productivity.

The fundamental reason behind this is likely to be a tenacious deflationary mindset that I mentioned earlier. Consumers remain reluctant to accept price rises despite the improvement in the employment and the income situation. Therefore, firms are cautious about raising prices due to their concern over losing customers.

Another likely reason is that the productivity of Japanese firms, mainly in the service sector, is low by international standards, and thus there is significant room for improvement. In fact, initiatives are widely being taken in the services and retail sectors such as enhancing efficiency of customer services, cutting back excessive services, and optimizing inventory management and delivery services.

Such efforts by firms in these sectors are encouraged in part by digital technology in recent years, including artificial intelligence and robotics. These measures to improve productivity are expected to produce positive effects in the long run in that they would address structural issues such as a decline in the working-age population and lead to boosting the growth potential of Japan's economy. After easing (inaudible) short run, however, they likely will reduce the upward pressure on prices.

I would now like to make three points from the perspective of monetary policy. First, wages and prices have been improving gradually under the powerful monetary easing over the past five years, although sluggishness remains. Base pay increases have taken hold again in Japan's economy, and the proportion of firms that have raised their base pay has been increasing steadily.

In addition, mainly in the service sector, where there is an acute labor shortage, moves to reflect the increased wage costs in prices have been spreading gradually. As medium- to long-term inflation expectations are projected to rise through the adaptive formation mechanism, if further price rises come to be observed widely the Bank of Japan judges that the momentum toward achieving the price stability target of 2 percent is firmly maintained.

Second, the bank therefore needs to maintain a positive outward gap by persistently pursuing powerful monetary easing, and as a framework of QQE, with yield-curve control. The bank thereby will encourage firms' wage and price setting stance to become more proactive and maintain positive momentum for a long time.

Third, sluggishness in prices is attributable to a rise in productivity that reflects technological innovation in recent years. It is important to continuously examine how this will affect the natural rate of interest as well economic and the financial activities. The effects of new technologies on the economy are often difficult to grasp in an accurate and timely manner using existing statistics. Thus they should be examined in detail from various perspectives.

MS. FLANDERS: Thank you. You've all focused on wages and wage growth…But I'm interested – Governor Kuroda, if I could just come back to you briefly – that Governor Lowe pointed out that even the 2 percent wage growth that they're seeing now in Australia was not enough to achieve the inflation target. How important is more wage inflation to you in hitting your target?

MR. KURODA: The Japanese government has been asking labor and business to raise wages in the last five years. And this year, the government even requested labor and business to agree to a 3 percent wage increase during the so-called spring offensive. The final result is not yet known, but I presume a total wage increase, including base pay as well as other elements of wages, would have risen close to 3 percent.

As I said, the Bank of Japan is aiming at achieving a 2 percent inflation target or a price stability target. While the labor productivity increase in Japan is around 1 percent, that means that a 3 percent wage increase is necessary to be consistent with a 2 percent price stability target. So the government request for a 3 percent wage increase is quite appropriate.

By the way, also the government has been raising minimum wages by 3 percent almost every year. And again, this is consistent with our price stability target.

MS. FLANDERS: Governor Lowe, I'm interested in the context – the conversations that we had yesterday about whether or not central banks can really change people's expectations and the difficulty of talking to households and really changing their way of thinking when they are often really not wanting to pay attention to you at all.

How do you think about your capacity to affect that wage growth? You say that's a major focus now. Is it harder to do that because we're so concerned about talking to markets that it's harder for us to talk directly to households?

MR. LOWE: Yeah, I'm not trying to talk directly to households on this particular issue. I'm trying to talk to businesses. We've got the situation where we've got the central bank governor calling for higher wage growth, the political leaders in a center-right government calling for higher wage growth and senior members of the business community calling for higher wage growth. You know, it doesn't happen.

And then when I talk to individual businesses, they kind of agree in principle the country would be better off having wage growth of 3-point-something, 3-point-something, but not any –

MS. FLANDERS: But then not being told what to do, though.

MR. LOWE: I'm not in their business. (Laughter.) And the reason that it shouldn't happen in their business is they're so worried about competition. You've kind of – in a market economy, we don't have the coordination mechanism to get to something which I think would be a better outcome because no individual business wants to put up its wages more quickly than its competitors. There's a first-move problem.

So the thing that I'm trying to do – and I don't know whether it's going to be effective – is to kind of help solve that coordination problem by saying, look, it's OK, it's OK to give wage increases of 3-point-something. And if that can become the norm, I think we'll be better off. And I don't know whether it's going to be effective or not.

MS. FLANDERS: President Draghi, I'm sort of interested. I mean, the eurozone experience of this is a little bit different and I guess not just because the recovery is not as far along as the many, many years' recovery in Australia. You know, we've heard a lot in the last couple of days and we just heard from Philip, there's something different about the wage-bargaining process at the moment and we're getting a lot of employment growth and not so much wage growth. And yet, if you look at the forecasts for the eurozone, it feels like we're not expecting such a transformation in the labor market outcomes, at least in many countries in the eurozone, maybe in some. We think the natural rate has fallen dramatically. How do you think about whether or not wage bargaining and the wage-employment relationship has changed in the eurozone?

MR. DRAGHI: Well, it's a difficult question because we actually have 19 countries and each one of them has a historical setup in those relations and I don't think they can be easily compared.

MS. FLANDERS: But you have to set monetary policy for all of them. (Laughter.)

MR. DRAGHI: That's right, exactly. And that's the challenge. But it's really changed, in a sense. As I was mentioning, one of the reasons in the list of why the wages are not responding as fast as we were used to is the disappearance of trade unions. Now, in some countries, they were important to begin with, but in others were not. So there is a combination of factors that has changed this relationship. But the point I was making before is that, yes, that's true, that explains the past.

We are convinced that the future looks different, looks much more like what we used to see years ago when this relationship was stable and we were looking at that to predict the movement in wages from the labor market conditions. So by and large, you have a variety of factors we think we are convinced that were very important in the past in explaining this low speed of adjustment, and now they are sort of washing out, they are less important. We see, for example, that – what was discussed in the first day of this conference – the residuals or Phillips curve washing out, moving away. The relationship is increasingly capturing a rather traditional design.

Now, of course, maybe – we've got to be careful here because maybe we're going to see – absolutely, we're going to see things that don't exist; and therefore, we convince ourselves that they exist. But frankly, if I compare, for example, all the projections about future inflation that the ECB has produced over the last four or five years, you clearly see a greater convergence, you clearly see a narrowing down on the confidence intervals, you clearly see an upward trend in underlying inflation.

For example, one thing that's telling is that, over our projection horizon, the underlying inflation – now, the core inflation is higher than headline inflation. So in our projections, we're actually discounting some slowdown in **oil prices**, but an underlying strength which remains through 2020.

So I would say, yes, I mean, it's a complex continent, 19 countries, very different, lots of reasons they can explain the past. Not sure that this diversity is what can – is the best predictor of the future.

MS. FLANDERS: We've been implicitly talking about as if we have many, hopefully, many more years of recovery to go and to discover what the dynamics of wages and prices will be, but we started the week with quite a provocative speech from (former U.S. Treasury Secretary Lawrence) Summers who said that the world was now economically, politically and socially less prepared for the next downturn than it's ever been.

Chairman Powell, do you agree with that?

MR. POWELL: Well, a couple of things we know are that interest rates have been lower. And they may – we don't know this, but they will probably remain low, which means we'll be closer to the zero lower bound, which may mean that we're more likely to hit the zero lower bound. And I think we've taken that into consideration.

I think there's still fiscal policy space in the United States. There's less than there used to be, there's less than there should be. But there's some room to react.

And I think we – I think we kind of take all of that onboard. And then the real question is – and I guess Larry (Summers) may have said something about this, I didn't pick that part up – but, you know, what's the right policy response to that?

And, you know, if you look at an economy in the case of the United States, which has growth well-above trend, unemployment at 3.8 percent, inflation moving up, not quite at target, but getting close, and the federal-funds rate still in a place that is accommodative in the view of members of the committee, perhaps a hundred basis points below the median estimate of a neutral rate. So what that calls for in our thinking is continued, gradual rate increases.

MS. FLANDERS: And I guess one of the things that came through in Larry Summers's remarks, but also other places, is that, because we know that there is this reduced monetary policy capacity, we expect there to be in the coming – next time we have a downturn, the relationship between fiscal and monetary policy becomes quite a lot more complicated in this environment where you have a lot more unconventional policy or potential for unconventional policies. I mean, even now, there's a potential for conflicts to develop between the fiscal objectives and the monetary objectives.

I mean, Governor Kuroda, I wondered, you know, how you think about the interaction between fiscal and monetary policy over the next few years in a – in a somewhat abstract way. But is it now more complicated than when we first designed those independent central banks?

MR. KURODA: Always the cooperation between fiscal authority and central bank by way of policy coordination or something like that is necessary. But at the same time, the mandate of the central bank is basically price stability and financial system stability. Of course, some central banks like the Federal Reserve and the Reserve Bank of Australia have another mandate of achieving full employment or something like that. But for the Bank of Japan, the mandate is basically price stability and financial stability. And we have to continue to aim at achieving and maintaining price stability and financial stability. And in some cases, that might make active or proactive fiscal policy somewhat difficult, but at this moment I don't see any difficulty of coordinating fiscal policy and monetary policy arising in the near future. I don't see any problem.

MS. FLANDERS: Well, I guess one example is if the government is now going to move to having a broad target for the budget deficit, which includes the debt interest. Then that complicates things for you a little bit.

MR. KURODA: Yeah, the government is aiming at achieving primary surplus by fiscal 2025 and also trying to achieve debt-to-(gross domestic product) ratio to gradually decline over time. And I think that (a) fiscal consolidation program is quite appropriate for the Japanese economy as well…because already the Japanese government has accumulated very large debt over the years and it's quite necessary for the government to consolidate (its) fiscal position, of course gradually, in the medium to long run. And that is not particularly inconsistent with our monetary policy in coming years.

MS. FLANDERS: I had one more question, for Chairman Powell.

We had some discussion yesterday – I think you weren't here for it, but there was some discussion about how central banks should communicate to households and whether perhaps we end up – talking a lot to **financial markets** means that you're also talking in a very careful – as you all are today – very careful way that then makes it harder for you to speak sort of directly and straightforwardly to households. You said in the – in the panel that we were – that you participated in recently when we were both in Stockholm, you said you thought that maybe there would be less room for – less need for forward guidance in the future. It made me think when Charles Wyplosz was saying you shouldn't be spoon-feeding the markets. You know, do you want to say a little bit more about how you see forward guidance?

MR. POWELL: Sure. So, obviously, we want the public and the markets to understand how we're thinking about the economy, how we're thinking about the path of policy, our reaction function, and that kind of thing. I think during the financial crisis, in order to support the economy, we began to do quite explicit date-based and then state-based forward guidance about the path of policy. And that was – that was, you know, an unconventional tool that we came to rely upon. I think it worked. I think it did assure the public that rates would remain lower and that sort of thing.

So, as we move back to a more normal environment in the United States, we're going to have a shorter statement at the end of the meeting that won't have so much in the way of formal forward guidance. We're still going to have the Summary of Economic Projections, which puts out quite a lot of information about the individual projections of individual members of the committee. So that's really how we're thinking about forward guidance – how I am, anyway.

Q: Lars Svensson, Stockholm School of Economics.

I have a question to Philip Lowe. He was nervous about the side effects of lowering the policy rate and raising inflation to the inflation target in Australia, nervous about the side effects of that. I would like to point out to another side effect of undershooting your inflation target. If you do that on a sustained basis, if you accept lower inflation on average than your inflation target, that is like having an implicit unofficial target below the official target. Once the market and the general public understands that, they will lower their inflation expectations. By the Fisher equation, that means that the average policy rate will then be correspondingly lower, and the gap to the effective lower bound will be shorter/smaller, and we will more likely hit the effective lower bound in the future. Doesn't that make the economy less resilient and more vulnerable? Isn't that a pretty important side effect of undershooting your inflation target?

Q: Ben Friedman from Harvard.

My question is for any or all of our distinguished panelists. The overwhelming focus of discussion at this conference has been about how the flattening of the Phillips curve has made and is making it more difficult for our central banks to raise inflation up to their stated targets. I hope each of you has been thinking about the reverse of that proposition, which is that in the event – we hope unlikely – that something goes wrong and we wind up with inflation above our central banks' targets, then, either because the central bank's policy is behind and – in slowing the economies or something goes wrong with **oil prices** – there's, of course, the usual laundry list of things that could go wrong – the same flattening of the Phillips curve we've been talking about would then make it more difficult for our central banks to reduce – to reduce inflation back down to the targets. And in a world of dynamic strategy for policy, surely that implication has some bearing on policy today. So I wonder whether our central banks have taken account of and are thinking about the potential difficulty in which they would find themselves should inflation for some reason or other over the next some years wind up being in a situation in which not how do we get from 1 to 2, but how do we get from 3 or something like that to 2.

Q: I'm Stefan Gerlach from EFG.

So my question is also to Philip Lowe, and it's along the line of Lars' questions. So, Philip, you mentioned that the public may not care very much if inflation is 1 percent or if it's 2 percent. But anyone who has borrowed is going to care about what the actual inflation is. In particular, governments are going to care. See, if they have – I mean, they borrow under the assumption that the central bank will deliver on the inflation target. And if inflation ends up being unexpectedly low, ex post real interest rates end up being unexpectedly high.

Now, that's not a problem if you have a public debt-to-GDP ratio of 40 percent, which I think is the Australian case. But it is a problem if the public debt-to-GDP ratio is 140 percent, which is the case in some countries. Now, one can, of course, argue that this is just an example of poor fiscal policy, and the central bank should simply disregard this. But in practice, I mean, shouldn't the central bank worry about the public finance consequences of running unexpectedly low inflation? Thank you.

MS. FLANDERS: Philip Lowe, do you want to answer those – the couple of questions that were particularly related to you? But then I think others will probably have remarks.

MR. LOWE: Thank you. Well, I acknowledge the risks that both Lars and Stefan talk about, but in my mind they're relatively marginal. Our fiscal policy kind of is – we've had excellent fiscal policy for a long time, so we don't have a public debt issue at all. And I remain confident that we are going to get back to 2 ½ percent, it's just going to take us a bit of time. And I accept that it's going to be a gradual process, and because it's gradual – because it's gradual, people might lower their inflation expectations. But if we keep communicating that we're shooting for 2 ½ and we're making gradual process towards that, I don't think we're going to see a persistent decline in inflation expectations.

There is a risk, though, that happens, balancing that risk against the risk that would come from pursuing a policy that pursued a more rapid return of inflation to 2 ½ percent. And in the environment we've been in, I see the risks being quite large from trying to get inflation up more quickly. We've been 1 ¾ to 2. I think we can live with that for a while. To try and get it back to 2 ½ very quickly, it wouldn't be mainly through people borrowing more money and having higher asset prices. I think that's a much bigger risk to our economy than people having surprisingly low inflation expectations. We've got very high levels of debt, very high levels of asset prices. And I think that is – that's our number-one domestic risk, not lowering – people having lower inflation expectations. We're trying to balance those two things off.

MS. FLANDERS: Do you want to respond to the point about the flatter – the flipside of the flatter Phillips curve?

MR. POWELL: I would – I would just briefly say, so, if we think inflation is held in place by relatively strongly-anchored inflation expectations, and we've seen years and years of inflation below that, the principal risk we've been worried about through these years is the pressure on inflation expectations, that they might move downward, which would be really bad in a – at a time when we think interest rates are going to be low. It would mean even less room for policy to respond. So that's been the thing we've been – we've been worried about. Not moving inflation up, but just really worried that we'd lose expectations.

So and I think as you get to a place where – as we're getting close now to on-target inflation, I think we're well-aware that if you go – if expectations were to move above 2 percent meaningfully then, yes, it would be some work to get it back. But that project – you know, we haven't really seen inflation expectations get up to 2 percent yet, or inflation itself.

MS. FLANDERS: Do you see any advantages to having inflation – when you've had a prolonged period below inflation – of having inflation that overshoots for some period of time, on this expectations question?

MR. POWELL: You know, that's not the design of our approach. We've said that we would be concerned if inflation were to run persistently above or below 2 percent. And so we haven't said what we're shooting for, and would like an overshoot. That's not something we've said. But I think – you know, as I said in my remarks, it doesn't mean that we can stop thinking about resource utilization. It really is just a question of keeping inflation expectations anchored at 2 percent.

MR. DRAGHI: First, to Lars, I mean, you will be able to guess that we've been asked several times to revise our objective of inflation. And it depends on whether you are located in eurozone. You have countries that was tasked to revising downwards – people, I mean, just not countries. Just not governments, but people saying – claiming that 2 percent was an outrageously high inflation. And countries that – people in countries that have been suggesting that 2 percent was too low inflation. One of the reasons why we refuse to – there are many reasons why it would have been unwise to advise our objective. But one of the reasons why we never revised the downward our objective was exactly what you said. We simply would self-limit our policy space without any clear gain from any point, from any angle. So there is no reason to do that.

On Ben's question, I think I'll say something very close to what Jay has just said. I think it's a high-class problem at this point in time. But we've asked ourselves what if. Of course, you know, if we are being questioned – we've been questioned so many times about the monetary policy being so unconventional, so expansionary, so accommodating, that we had to ask ourselves what if. And the answer is that we have plenty of instruments to do that. We have plenty of instruments to go back. And certainly, our deposit facilities is one that comes to mind immediately. The rhythm of the investment policies is another one that comes to mind. A third would be interest rates, in due time.

So but there is also another observation that came to mind while you were asking the question is: Are we sure that the slope of the Phillips curve remains constant in an entirely new regime of inflation, where expectations are being adjusted to a permanently higher level of inflation? And I'm not sure I would answer yes, because one of the reasons – one of the things that – one of the reasons why we find it so difficult to disentangle different factors is exactly we are unsure that that it's been stable throughout the last 10 years – the slope, I mean.

That's the – the other thing we look at, however – and that also gives guidance to the responding to your question – is we have very different countries in the eurozone. And they are different for a variety of reasons, one of which, however, is relevant to this discussion is how advanced are they on the recovery path? What's their position in the business cycle? And ideally, what we would like to see is higher inflation for countries that are in different – higher, but different inflation rates for countries that are in different positions in the business cycle. And we are seeing some of that, which is another encouraging sign that are proceeding on a convergence path.

MS. FLANDERS: I'm interested, when you say you have lots – plenty of facilities, plenty of instruments – I mean, on most of – it goes back to the point earlier, on most of the estimates of when we might have a recession, a lot of those instruments are not going to allow the kind of room that you had in response to the crisis. I mean, don't you think there will have to be more of a role for countercyclical fiscal policy in that environment?

MR. DRAGHI: Oh, OK, no, but Ben was talking about the opposite problem, namely too high inflation. No, you are –

MS. FLANDERS: Right, but don't you sacrifice –

MR. DRAGHI: Again, what do we do if we have a recession? Well, frankly, even on our medium-term horizon projections, namely until 2020, we don't see a recession. We see – we see lower growth, but nothing that resembles to a recession. So the question is sort of should we actually ask ourselves what we would – not we, actually, not monetary policy. What others would do just in case of a recession. And here, again, it's very difficult to answer in a complex place like eurozone. So you have countries that have fiscal space and countries that don't have fiscal space. And here comes a completely different set of considerations. How do we – how do we ensure that the eurozone becomes gradually somewhat resembling to an optimal currency area? How do we assure that there is a collective convergence? And here, we enter in the sort of the realm of the reform of the monetary union, the deepening of the monetary union.

By the way, on this front, the recent document produced by France and Germany is to be welcome – is to be welcome, because it's an encouraging step in this direction. And it's an important step, made important by the very difficult political circumstances in which this document is being produced. And so that is – and it's also important – it's been made important because I think, if I'm not mistaken, it's the first time we are having a proposal by governments. So we had proposals by the commission. We had proposals in the famous Five Presidents' Report, but they were not governments' proposals. And this is – but we cannot – bottom line of the answer I'm giving to you, we cannot disentangle what would be the policy response in front of a so far hypothetical big recession in the euro area from the question of the reform of the deepening – what we call deepening of the monetary union.

MS. FLANDERS: Just quickly on what you said about the statement, because obviously that's a very timely thing to talk about: Is your interpretation of that agreement that it takes the eurozone closer to having a greater ability to respond fiscally to a future crisis?

MR. DRAGHI: You see, your question can be answered in a variety of ways. And some people would agree with this statement saying, yes, we need a stabilization capacity; others would not.

The important thing that I would draw from this recent development is that not necessarily a specific instrument is being designed, presented, and defined, but it's an approach. It's a – it's a sense that in the future we have to work to deepen the monetary union. Whether this instrument is exactly what you are suggesting, a stabilization budget, or it is an unemployment insurance scheme like has been suggested – hinted at, at least in the document – by the way, we shouldn't – I mean, the document is vague, as you've seen, so much work will be needed on that – it's going to be determined.

The important thing, in my view, is that for the first time, after discussing for several years the deepening of the monetary union, now finally we have something we can work on. And this something doesn't come from five presidents, individuals, but it comes from governments – from the German and French government.

Q: Mario Marcel from the Central Bank of Chile.

President Draghi made reference to underlying inflation and core inflation. And it seems odd to me that we have been discussing price dynamics over a couple of days and very little reference has been made to core and underlying inflation, which is quoted by central banks very often in justifying their decisions. So maybe one reason for that is that the most common measure of core inflation that we have, which is excluding food and fuels, may be too crude as a – as a measure of core inflation. So I wonder how much of what we have discussed these days about – you know, about building alternative price – inflation indicators may be already integrated into the kind of analysis that central banks make. Particularly, President Draghi has made reference on a number of calculations that are made by the ECB.

And a second question is that we have discussed a number of factors that may be pushing inflation down, some of which look like a one-off. But given that there may be a number of those, their effect may be more lasting. But I wonder of how would you react to another one of change in prices, which is raising import tariffs. How would you look at that in terms of measuring inflation and the response of monetary policy?

Q: Thank you. So in the past week just gone we saw the Federal Reserve retire forward guidance that had been in the statement for a long time and we saw the ECB introduce a new form of forward guidance. So I wanted to just take the opportunity to invite both the chairman and the president to comment on what they think we've learned about forward guidance. Specifically, when it is appropriate to use forward guidance? And at what point in the policy cycle does it become, if at all, inappropriate to provide this forward guidance?

MS. FLANDERS: So there was a question about the price-setting that happens from tariff-setting. I guess the broader question coming out of things like even the retaliation that we had announced today from the European Union is, you know, when does this trade issue become a real – start to have a meaningful impact on your assessment of the strength of the global recovery and potentially monetary policy going forward? Chairman Powell?

MR. POWELL: That's your question for me? (Laughter.)

MS. FLANDERS: Well, no, the question – he mentioned – there was a mention of trade. I was just clarifying.

MR. DRAGHI: I can take the import tariffs questions, if you want, and you take the forward guidance – because after all, you lifted it, we don't. (Laughter.)

MR. POWELL: Sure.

MR. DRAGHI: What is being projected in our – in the last set of projections are the tariffs that have been implemented already, which are not very – don't have a very significant effect, either on output or on prices. A completely different analysis would probably be – and, well, we haven't done it yet – when we will consider the tariffs that have been announced or implemented since then, first.

Second, the – it's not easy, but I think at some point we will have to figure out kind of what is the potential – what is the round retaliation effects that's going to take place? And what is the effect – and that's probably the most important thing – what's the effect on confidence? And therefore, what's the effect on business investment? What's the effect on experts? What's the effect on consumers' confidence? We think there have been lessons that one can learn from the past, and they're all – they're all very negative.

So it's not – it's not easy and it's not yet the time, in a sense, to see what the consequence of monetary policy of all this can be. But there is no reason – there's no ground to be – to be optimistic on that. The – on underlying inflation – oh, I'm sorry. Why don't you answer the other question, then I'll answer the underlying inflation?

MR. POWELL: On trade? Yeah. So, first, I'm obviously not going to comment on any particular trade policy, but in principle changes in trade policy could cause us to have to question the outlook. So we have a very wide range of contexts in the business world, in the United States, and around the world. And as we talk to them, they continually and increasingly express concern over trade developments. We talk about that in the beige book, and then the reserve bank presidents talk about it in the (Federal Open Market Committee) meeting. And we talk about it then in the minutes. And I'd say that those concerns seem to be rising. For the first time, we're hearing about decisions to postpone investment, postpone hiring, postpone making decisions. That's a new thing.

If you ask, is it in the forecast yet, is it in the outlook, the answer is no. And you don't see it in the performance of the economy, and we don't have any way to know how to put it into the – into the outlook just yet. So that's where that is.

MS. FLANDERS: Before we get onto the forward guidance, I'm sort of interested in what Governor Kuroda and Governor Lowe have to say on the trade point, because there's a perception that the countries that are more involved in with China will have less – will have some protection from this.

MR. KURODA: Yeah. I mean, rather than direct impact on the Japanese economy the indirect impact on the Japanese economy could be quite significant. If this escalation of tariffs by the U.S. and China continues, and actually implemented, that would significant affect the East Asia supply chains, centering on China, Korea, Japan, Taiwan, as well as Southeast Asian economies. So I really hope that this escalation could be rescinded and normal sort of trading relationship between U.S. and China would prevail. So this is a matter of great concern for Japan.

By the way, I just would like to make one comment on Professor Friedman's question, quite interesting question. Although, I mean – if really inflation rates suddenly accelerate toward 3 or 4 percent, by what factor, if it is through external factors, like sudden currency depreciation or sudden **oil price** rise, they would have only temporary impact unless the exchange rate continued to depreciate or **oil prices** continued to rise. So these are temporary factors, so I don't think this would raise a serious problem.

A sudden rise in inflation expectations, that is extremely unlikely. And then you would find that, after all, the Phillips curve was not so flat, the Phillips curve became steeper so that with a tight labor market the wages and prices started to rise, inflation accelerated and so on and so on. Then, of course, you can use a steeper Phillips curve to contain your inflation.

MR. LOWE: Well, on trade, I think what's happening is incredibly disturbing. Can any of us think of a country that's made itself wealthier and boosted productivity growth by building walls? Probably not. I can think of a lot of countries that have made themselves wealthy or more prosperous by reducing walls to people, capital, goods and services. And my country would probably be kind of the posterchild there. So I view what is happening as incredibly worrying.

The tariffs themselves I don't think kind of are going to derail the global expansion, but I can think of two mechanisms where the expansion could be derailed. The first is through **financial markets** because they're very good at telescoping future events to today. So far, the **financial markets** have taken a relatively kind of benign interpretation, but that could change very quickly, and so we could see a lot of turbulence as people bring those future events forward to today.

And the other mechanism is that businesses – the option value of waiting goes up a lot and kind of what Jay was saying, kind of people saying, to delay decisions. And in Canada, that's happening. In Mexico, it's happening. Disturbing that it's happening in the United States. It's probably happening in China. I know it's happening in parts of Southeast Asia. So the option value of waiting is very high at the moment, and it wouldn't take that much for **financial markets** to kind of combine with businesses who are waiting to turn this into a really big global event. So I hope that it has a low probability, but I'm very disturbed at what is happening and I think it's very worrying.

And so on a much smaller issue, on underlying inflation, I agree with Mario about the importance of looking at underlying inflation. And much of our public communication is around measures of underlying inflation, not the exclusion-based ones where you exclude food and energy, but we put a lot of weight on the trimmed mean measure of inflation and the weighted median. And much of our public communication is focused on those two measures.

MR. DRAGHI: Yeah, on the steel and trade and on the discussion of tariffs, there is a more general aspect of what is happening that it's, in a sense, if possible, would be even more worrisome, and that is the, I would say, the desire for unilateral action that has caught several countries, not only the United States. And, yes, we're talking about that in the context of tariffs, but there are other examples of unilateral action that basically undermines the multilateral framework in which, I believe, all of us have grown up.

And so the potential changes that this may start are something that is unknown. It's very worrisome. And again, I cannot see any positive side to that. So it's also a considerable – let me use the word that we use with markets, not with people: uncertainty.

MS. FLANDERS: And there was a question about the lessons of forward guidance.

MR. POWELL: Sure. So fundamentally, as we all know here, even on a good day, there's a tremendous amount of uncertainty about the path of the economy and, hence, the path of policy. And so to be providing a lot of forward guidance all the time is to risk under-communicating about that uncertainty. And I think that's a real risk for us, is to – that we say things and they're often taken as forecasts or even promises and they're really not. So I think in the ordinary course, we should – we should be very careful to communicate as clearly as possible about the level of uncertainty that we have. And I think explicit forward guidance kind of cuts against that.

But in a situation where the central bank needs to correct the public's misperception of the path of rates or needs to provide more accommodation and perhaps is close to the zero lower bound, I think that forward guidance is a very close end-product extension to just regular rate policy. It doesn't have political economy issues with it. It's sort of a commitment technology in a way, even though you probably will wind up saying that it's not a commitment, but the public, we know, will take it as such, to some extent.

And I think it works. I think the record in the crisis was that it did reduce uncertainty about the path of policy and even pushed down expectations about the best path of policy. So a relatively close end-product extension that I would think could well be used in the future when needed, but shouldn't be used in the ordinary course.

Q: Erik Nielsen of Unicredit.

Chairman Powell, last autumn in Washington, you gave a very good speech predicting that the Fed could normalize rates without having any negative impact, material impact on emerging markets. Since then, a few things have happened. You got a big fiscal expansion that sucks up a lot of savings from around the world, you have started to reduce your balance sheet, and you have become chairman. (Laughter.) And then we have had a bit of wobbles in emerging markets. I don't think anybody thinks it's systemic, but it's – but it's certainly out there. So I wonder whether you would sort of expand a little bit on whether you are as confident in what you said at the conference in Washington, today, or whether there is a bit out there that worries you a bit more. The yield curve has flattened a lot, which is, for us in the markets, something we kind of look at and wonder whether that's a forewarning or something more serious.

MR. POWELL: OK. Well, so on emerging markets, I should start by saying that emerging market economies now amount to more than half of economic activity and well more than half of the growth. So they're quite important and important to us. And, you know, the fact that they – having them remain strong is quite important to our own growth, so we recognize and appreciate that.

We also understand that in a world of global capital markets and integrated capital markets and integrated value chains and economies, the things that we do will have spillovers into other – through financial conditions, into other economies. And by the way, vice-versa, of course, as you have seen over the last couple of years.

So, you know, we tried – we understand that. And we know particularly that open – smaller open economies in particular can receive flows at times, which are – which make life difficult. It can be a difficult challenge for them to manage.

So what do we control about that? We control – one thing we control is to try to communicate as clearly as possible about how we see our economy and how we see the path of policy, how we would react to changes in either of those things.

And I think over the last couple of years, if you look back at over the last two years, where we are today is pretty consistent with what we've been saying where we thought we would be now and the way we thought we'd react. So that we do control. And we'll obviously – we'll continue to try very hard to, you know, to carry out our mandate and to avoid surprises wherever possible.

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WSJ PRO CENTRAL BANKING

Economy
Powell Says Solid Economy Supports Further Fed Rate Increases; Fed chief says keeping labor markets too tight could raise inflation expectations

By Nick Timiraos
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Federal Reserve Chairman Jerome Powell said sturdy U.S. economic growth has built a strong case for continuing to gradually lift interest rates, and he warned against policy complacency now that the central bank has nearly achieved its employment and price stability goals.

"Today, with the economy strong and risks to the outlook balanced, the case for continued gradual increases in the federal-funds rate remains strong and broadly supported among" participants on the Fed's rate-setting committee, Mr. Powell said Wednesday.

The Fed's rate-setting committee unanimously agreed last week to lift the central bank's benchmark short-term rate for the second time this year, to a range between 1.75% and 2%, and officials penciled in two more rate increases this year.

Mr. Powell spoke at the European Central Bank's annual policy conference in Sintra, Portugal. His prepared remarks highlighted the risks of allowing unemployment to fall too far below the level expected to prevail over the long run. Currently, Fed officials estimate that natural level of employment would put the jobless rate at around 4.5%, above the 3.8% unemployment rate recorded in May.

Mr. Powell said he saw few risks of bubbles but flagged how the prior two U.S. economic expansions ended after the eruption of financial imbalances, in the technology sector and the housing market, respectively, rather than overheating from excessive inflation.

"We have often seen confidence become overconfidence and lead to excessive borrowing and risk-taking, leaving the financial system more vulnerable," he said.

Few questions loom larger for the Fed than how low the U.S. unemployment rate can safely go. If it falls any further, it will stand at its lowest levels since the late 1960s, when sustained low levels of unemployment were followed by large increases in inflation that proved difficult for the Fed to contain.

Mr. Powell's speech flagged the uncertainty facing the Fed because of a limited sample of episodes resembling the economy's current situation. He said the example of the late 1960s wasn't as useful as policy makers might have hoped because the economy has changed significantly over the last half-century.

"The historical comparison does not shed as much light as we might have hoped," he said.

Today's economy has more college-educated workers than in the past, which depresses the natural rate of unemployment because they have lower unemployment rates than others.

Mr. Powell also said he was hesitant to draw too many lessons from the low-unemployment episode from the late 1960s because people now expect inflation to remain stable, reflecting in part the Fed's success in keeping prices stable in recent decades.

In the 1960s and 1970s, if inflation went up one year, consumers expected it to rise by at least as much the following year. Officials believe such expectations can be self-fulfilling as workers demand pay increases and businesses raise prices in anticipation.

Still, Mr. Powell warned against turning complacent in assuming that stable inflation expectations would prevent growing pressures should unemployment fall lower. Inflation expectations have been stable "because central banks have kept inflation under control," Mr. Powell said.

"If central banks were instead to try to exploit the nonresponsiveness of inflation to low unemployment and push resource utilization significantly and persistently past sustainable levels, the public might begin to question our commitment to low inflation, and expectations could come under upward pressure," he added. Mr. Powell said there were no signs of this currently happening in the U.S.

Fed officials largely follow a framework that suggests an inverse relationship between inflation and unemployment, known as the Phillips curve. But this relationship hasn't been strong over the past 20 years, meaning big swings in unemployment haven't significantly affected inflation.

While this relationship suggests "the implications for inflation might not be large" if unemployment runs below the estimated natural rate for an extended period, Mr. Powell said it was possible a "very tight labor market could lead to large, nonlinear effects," meaning inflation could still rise more rapidly once unemployment remains at a low enough level for a long enough time.

Another example of Mr. Powell's **bullish** view: In his opening remarks, he didn't address any of the reasons other Fed officials have cited recently for a potentially slower pace of rate increases, such as instability abroad or a narrowing in the spread between short- and long-term interest rates in bond markets.

Later, asked whether recent turmoil in a handful of emerging markets might lead the Fed to reassess its plan to raise rates, Mr. Powell offered few specifics, and little to suggest any immediate reaction. He said emerging markets were an important source of global growth and therefore an important consideration in the Fed's assessment of the economic outlook, and he said the Fed could be most helpful by speaking clearly about its policy intentions, which he said it had done in recent years.

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THE WALL STREET JOURNAL.

Business

Starbucks Shares Slide as Company Plans More U.S. Store Closures; Stock is the worst performer in the S&P 500 and on track for its lowest close since November 2016

By Julie Jargon
463 words
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Starbucks Corp. said it would close more coffee shops in the increasingly crowded U.S. market where it was a pioneer, sending shares sharply lower in trading Wednesday.

The company said the need for closures was driven in part by slowing sales in the U.S. Starbucks said Tuesday that it expects global same-store sales growth of just 1% in the current quarter, well below analysts' expectations of 2.9% growth, due not only to the weakness in the U.S. but also to worsening sales in China.

On Wednesday, shares of Starbucks fell nearly 9% to $52.50 in midday trading, and the stock was the worst performer in both the **S&P 500** and the **Nasdaq** 100. If the slide continues, it could result in the lowest market close for Starbucks since November 2016.

The coffee giant said late Tuesday that it would close 150 U.S. stores in its 2019 fiscal year, triple the number it has closed on average in recent years. Starbucks said it also will slow the growth of licensed stores in airports, supermarkets and other retail stores, reflecting criticism that the coffee-shop pioneer was expanding too rapidly.

Sales at Starbucks stores in the U.S. have been slowing in recent years. Late last year, Starbucks reduced its long-term sales and profit targets. In April, Starbucks reported that traffic to its U.S. stores was flat in its fiscal second quarter.

Starbucks Chief Executive Kevin Johnson said his company still has room to grow in some parts of the U.S., such as the Midwest and the South. Most of the stores that will be closed are in more urban parts of the country where Starbucks stores are tightly clustered and where rent and wages are high, he said.

At an investor event on Tuesday, Mr. Johnson, who became chief executive last April, also sought to draw a distinction between his plans and those of Howard Schultz, the longtime CEO who recently said he is stepping down as chairman later this month. Mr. Johnson said he is more data-driven and analytical than Mr. Schultz.

Mr. Johnson said he plans to increase same-store U.S. sales by expanding the company's "digital relationship," with customers, which it has begun to do by opening its mobile order app to guests who aren't members of its rewards program. The chain also is giving rewards points to non-rewards customers who register a credit or debit card with the company.

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The New York Times

Business Day; DealBook
G.E. Dropped From the Dow After More Than a Century

By Matt Phillips
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English

And then there were none.

General Electric, the last original member of the **Dow Jonesindustrial average**, was dropped from the blue-chip index late Tuesday and replaced by the Walgreens Boots Alliance drugstore chain.

The decision is a fresh blow to General Electric, which has stumbled badly in recent years. Last fall, John L. Flannery, the company's new chief executive, warned that the power-generation unit was reeling. G.E. cut its dividend for only the second time since the Great Depression. In January, G.E. surprised investors by taking a big charge and setting aside $15 billion over seven years to pay for obligations held by GE Capital, the company's financial services unit, mainly on long-term care insurance policies.

[Read about Mr. Flannery's goal to make G.E. "simpler and easier to operate."]

Over the last year, G.E.'s shares have fallen 55 percent, compared with a 15 percent gain for the Dow. G.E., which closed Tuesday at $12.95, has the lowest share price of any of the index's 30 components.

S. & P. Dow Jones Indices — which owns the Dow — suggested that the slide in G.E.'s **stock price** contributed to the decision to remove the company from the index, where it had been a member continuously since 1907. The Dow is a price-weighted index, which means higher priced stocks have a greater influence on its direction.

"The low price of G.E. shares means the company has a weight in the index of less than one-half of one percentage point," said David Blitzer, chairman of the index committee at S. & P. Dow Jones Indices. "Walgreens Boots Alliance's share price is higher, and it will contribute more meaningfully to the index."

The move also is freighted with economic symbolism. With the inclusion of Walgreens Boots, the index "will be more representative of the consumer and health care sectors of the U.S. economy," Mr. Blitzer said.

The removal of G.E., which will formally occur June 26, reflects a shift in the economic composition of the United States, which long ago tilted away from heavy industry and toward services, such as technology, finance and health care.

And it also amounted to a milestone for General Electric. It was the last remaining original member of the index, when the **stock market** measure was introduced in 1896.

Back then, just a few years after the company was formed through a merger of Thomas Edison's electric companies with a rival, G.E. was the modern-day equivalent of a technology stock, and the Dow itself was geared heavily toward the growth industries of the day such as railroads. In the more than 120 years that followed, the company was often at the center of American capitalism. And as recently as the 1990s. G.E. was at times the most-valuable American company by market value.

[G.E. mirrored the growth of industrial America from the steam age to the age of electricity and beyond.]

Alphabet, Amazon, Apple, Facebook and Microsoft are the five most valuable companies in the United States today.

After G.E.’s departure from the index, the company with the longest presence in the Dow will be Exxon Mobil, whose corporate predecessor, Standard Oil of New Jersey, joined the Dow in 1928, according to S. & P. Dow Jones Indices.

General Electric, the last original member of the **Dow Jones industrial average**, was dropped from the blue-chip index. | John Minchillo/Associated Press

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THE WALL STREET JOURNAL.
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Fed's Tightening Has Investors on Edge --- As the central bank pares bondholdings, riskier assets globally hasten their slide

By Daniel Kruger
773 words
20 June 2018
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The Federal Reserve's move to trim the size of its bondholdings has exacerbated recent declines in prices for risky assets around the world, investors say.

The central bank has scaled back its mountain of Treasury and mortgage debt by $111.9 billion since the policy was announced in September.

More than half the reduction has taken place since the end of March, and the process of withdrawing money from the economy is scheduled to reach $50 billion a month in October.

The Fed's balance sheet swelled to $4.5 trillion in the wake of the financial crisis as the central bank bought government and mortgage debt in hope of kick-starting growth.

Now, with the U.S. economy on firmer ground and unemployment at its lowest levels in decades, the Fed is removing that stimulus by allowing some of its holdings to mature without reinvesting the proceeds.

Some analysts and investors said the moves heightened **volatility** that spread through government bond markets earlier this month due to economic problems in countries such as Brazil, South Africa and Turkey. Currencies of those countries have declined against the dollar by roughly 12%, 13% and 16%, respectively, since the end of March.

In turn, worries about those countries fueled demand for safer assets including Treasury debt.

"The markets are more discerning" about what kinds of risks are acceptable, said Robert Tipp, chief investment strategist at PGIM Fixed Income. The disruptions from the shrinking of the Fed's balance sheet "are going to be felt in proportion to" the weakness of each market, he said.

An added worry is that besides balance-sheet actions, the Fed also has been raising short-term rates. Some investors believe it is natural for assets at relatively elevated valuations, such as stocks, to come under pressure when the Fed is in tightening mode. That is especially true as the economic expansion enters its ninth year.

Several investors expect the shift away from risky global assets to become more pronounced over time as the Fed reinvests in less and less debt. Meanwhile, the European Central Bank said last week that it would stop buying bonds outright in December, although it will reinvest proceeds of bonds that mature in its portfolio.

Shrinking the Fed's balance sheet will reduce foreign purchases of emerging-markets stocks and bonds by about $70 billion combined in 2018 and 2019, according to estimates from researchers with the International Monetary Fund. That is a contrast to average annual inflows of $240 billion since 2010.

Those inflows occurred as the Fed was expanding its balance sheet, which encouraged investors to take on more risk.

Now that the trend is going the other way, the effect of the Fed's move to shrink its holdings has caught the attention of some foreign policy makers. These include the heads of the central banks of Indonesia and India. Indonesia raised interest rates twice in May, in part to support its currency against a rising U.S. dollar, while India raised rates in June. Bank of India Governor Urjit Patel urged the Fed to slow down.

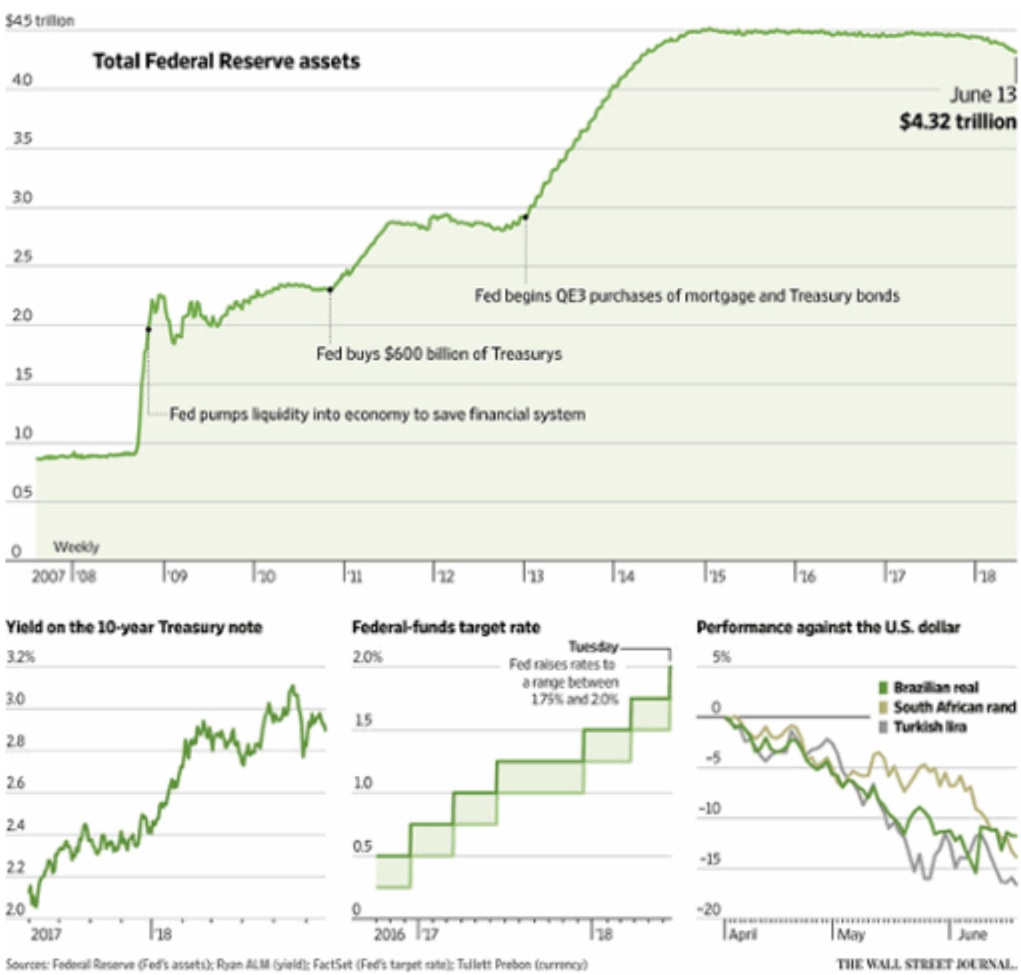
Mr. Patel said in an opinion piece in the Financial Times early this month that the Fed's balance-sheet reduction was making it harder for emerging markets to handle a dollar liquidity squeeze. This is being driven largely by U.S. fiscal policy -- namely, the increase in Treasury debt issuance to cover widening federal budget deficits. At the same time the deficit is rising, the Fed is shrinking the supply of dollars, contributing to a shortage.

Some analysts blame recent **volatility** on the dollar's rise. Many investors had bet on the U.S. currency declining in value against the euro, furthering a trend seen in 2017. That hasn't worked as planned this year, compelling investors to reverse trades as Europe's growth has lagged behind the U.S.

Tighter policy from the Fed has been "ultimately the most important factor," in the performance of global markets, said Holly MacDonald, chief investment strategist at Bessemer Trust, which is overweight U.S. securities. "Right now there's not a whole lot of compelling opportunities in global fixed income."

As the Fed continues to shrink its bond portfolio, "this is probably the biggest risk," Ms. MacDonald said. Investors are looking over their shoulders because shrinking liquidity helps intensify market spasms.

"It's underlying the backdrop of the **volatility** we're seeing this year," she added.



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THE WALL STREET JOURNAL.
U.S. EDITION

Opaque Pricing Puts the Brakes on Market for Hot Metals

By Amrith Ramkumar
688 words
20 June 2018
The Wall Street Journal
J
B13
English

Investors in two of the hottest commodities in recent years face a vexing problem: Reliable prices for lithium and cobalt are every bit as rare as large deposits of the valuable ores.

Interest in the materials has soared on expectations that demand will rise as they are used in a rapidly expanding number of electric-car batteries. The market for the two metals has already jumped to as much as $10 billion from about $4 billion two years ago, according to estimates. Analysts project that figure could double again by 2025.

But unlike most other commodities, lithium and cobalt don't have actively traded futures contracts tied to them. That means many investors are forced to rely on costly services that give price estimates, market participants say. But analysts say even those figures can differ from the privately negotiated prices used by large miners and Chinese battery manufacturers, deals that make up a significant chunk of the market.

That is bad news for a nascent market that is already prone to rapid price swings. The Global X Lithium & Battery Tech ETF is down 16% this year after a 59% surge in 2017. Supply and demand projections for lithium and cobalt can move significantly because they are tied to how quickly consumers will adopt electric cars, a trend that skeptics say is largely built on hype given the history of disrupting long-entrenched habits like driving.

All this raises the risk of unexpected **volatility** in prices. While investors are starved for growth and returns after years of low interest rates, the opacity in metal prices and fickle market sentiment are keeping some away even as large companies like SoftBank Group Corp. and Tesla Inc. make investments. It is why asset-management firm Fiera Capital Corp. hasn't invested in producers of the metals, said Nick Page, a portfolio adviser for Fiera's European division.

"The market is quite opaque," he said. "It's difficult to take any comfort from all of the different forecasts, which makes it more risky."

Analysts say the situation benefits the biggest players in commodities, like Swiss trading firm Glencore PLC, the world's largest cobalt supplier, and global chemical companies Sociedad Quimica y Minera de Chile SA and U.S.-based FMC Corp. and Albemarle Corp. Those firms have existing relationships with refiners and battery makers concentrated in China, the industry's dominant player.

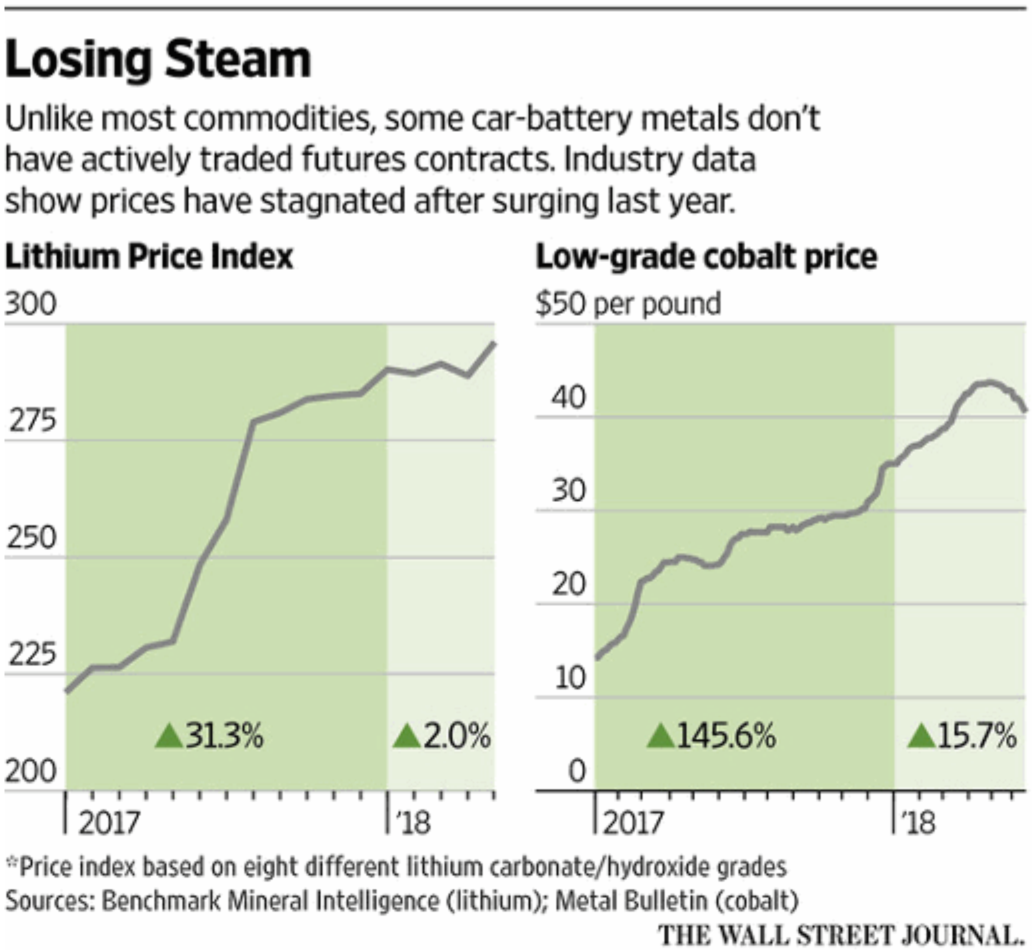
While it is true that in other assets big players also tend to have information advantages, it is especially dangerous for small producers and investors in markets like lithium and cobalt that are defined by largely speculative bets on supply and demand. That risk could limit investment in the industry, some analysts said.

"Without going to China to see all the demand for battery materials, it's really hard to get a handle on it," said Mathew Lazarus, managing member at New York-based hedge fund Red Hook Asset Management LLC, which owns shares of several lithium producers. "That's the gating item, that investors have to take a leap of faith that there's going to be all this demand when we can't see it."

Finding dependable prices is more challenging for the materials than other commodities because they have to be refined into chemicals like cobalt sulfate or lithium hydroxide, adding to the complexity because of the multitude of chemical grades and varying prices for them.

Even the London Metal Exchange has struggled to launch contracts for lithium and cobalt with standardized and transparent pricing. Some market participants use the LME's physical cobalt metal contract as a proxy, and the exchange said last October that it was looking into cash-based contracts for lithium, cobalt and nickel compounds.

But an LME spokeswoman confirmed to The Wall Street Journal that some of these efforts have been abandoned because of a lack of demand for some chemical compound contracts. The exchange is still working on a cobalt contract using cash and a lithium contract, the spokeswoman said.



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THE WALL STREET JOURNAL.
U.S. EDITION

Innovations in Finance (A Special Report) --- The Personalized Index Fund's Time May Be Near: Many people may not be up to the task, but some experts expect more individuals will be doing this

By Chuck Jaffe
1,015 words
20 June 2018
The Wall Street Journal
J
R7
English

Someday soon, your favorite index could be, literally, "the index of my favorite stocks."

While you might not feel qualified, technology already exists to help you build an index just as good as what the experts do, and lower your investment costs in the process.

"Personalized indexing" may not be here yet, but it isn't far off.

Index investing and passive management -- buying and holding a basket of stocks that replicates a benchmark -- has been taking over the investment scene for years. Index funds attract the vast majority of investment flows, compared with active funds. Their low cost, transparency and tax efficiency are the pillars of the multitrillion-dollar exchange-traded-funds business.

Yet what investors have seen is just the beginning.

Whatever the financial-services industry can dream up, and believes the public will buy, it can turn into an index ETF. That is why there already seems to be an index ETF for every occasion and specialty, from artificial intelligence (AIEQ) to gaming (GAMR) to obesity (SLIM) to whatever stuff millennials are into (MILN).

It isn't a big step from that to building an index portfolio that follows your personal rules.

As indexing has evolved, so has the thinking about what index funds are and what they are supposed to do.

Jack Bogle, founder of Vanguard Group and the first index fund, advocated classic indexing, where investors buy into old-school indexes like the **S&P 500** and hold them forever. This is truly "passive investing," where both the buyer of the fund and the manager of the fund do virtually nothing.

But many investors these days are "tactical," meaning they trade passive index funds to tilt a portfolio toward whatever sector or region is most promising at any point. As investors, they could be described as "actively passive."

The next extension of this phenomenon becomes the personalized index, one where you make the rules.

While it could be as simple as "buy all large-cap stocks with a positive earnings trend and no debt on the balance sheet," it is more likely to reflect research you trust, with your confidence then leveraged into a portfolio.

Here's how it might work: You go to your brokerage website, logging into the research tools there from your favorite analytical firms, like Morningstar Inc. You screen investments -- mixing and matching what you want to see. You cross-reference different research firms, maybe combining 5-star options from Morningstar with highly rated securities from other research firms and add in personal criteria, like a preference for increasing dividend payouts.

It's a rules-based approach where you make the rules.

Ben Johnson, director of global ETF research at Morningstar, compared the financial concept to what hungry eaters find at Chipotle Mexican Grill: "All of the ingredients are out there, and you order whatever looks good to you, and each person gets their food the way they want it, at a cost they can see and understand. You get exactly what you want."

With the screening done and the rules in place -- including how often to rebalance and how to weight the portfolio -- you click a button to buy the portfolio and -- boom! -- personal index fund.

There will be trading costs to buy the securities -- currently excluded from the expense ratios of traditional funds and outside of the cost structure of ETFs -- but no management fees. And brokerage firms are developing ways to nearly eliminate trading costs, such as flat annual fees for managing a personalized portfolio.

"The technology is here to do it now, but the industry is resisting it because the establishment gets paid to put together baskets of stocks," says David Trainer, president of New Constructs, a Nashville-based research firm. "As cheap as index funds are, the truth is that investment firms have been overcharging people for simply putting stocks into groups. You don't need that middleman anymore, so you will either buy the lowest-cost index funds out there or you will make them and execute them yourself."

Mind you, personalized funds aren't a new concept.

At the height of the internet-stock bubble, various firms started trying to sell investors custom baskets of stocks. The idea was to build low-cost, diversified portfolios where the investor knew, and controlled, all holdings. While the concept was supposed to democratize investing, the leading players moved where the money took them, away from the personalized funds angle and more toward menus of thematic, prepared portfolios.

It's worth remembering, however, that both indexing and the ETF industry didn't become popular concepts overnight. The first ETF opened in January 1993; it took more than 15 years for the industry to reach 1,000 offerings, then took less than 10 years to double from that size.

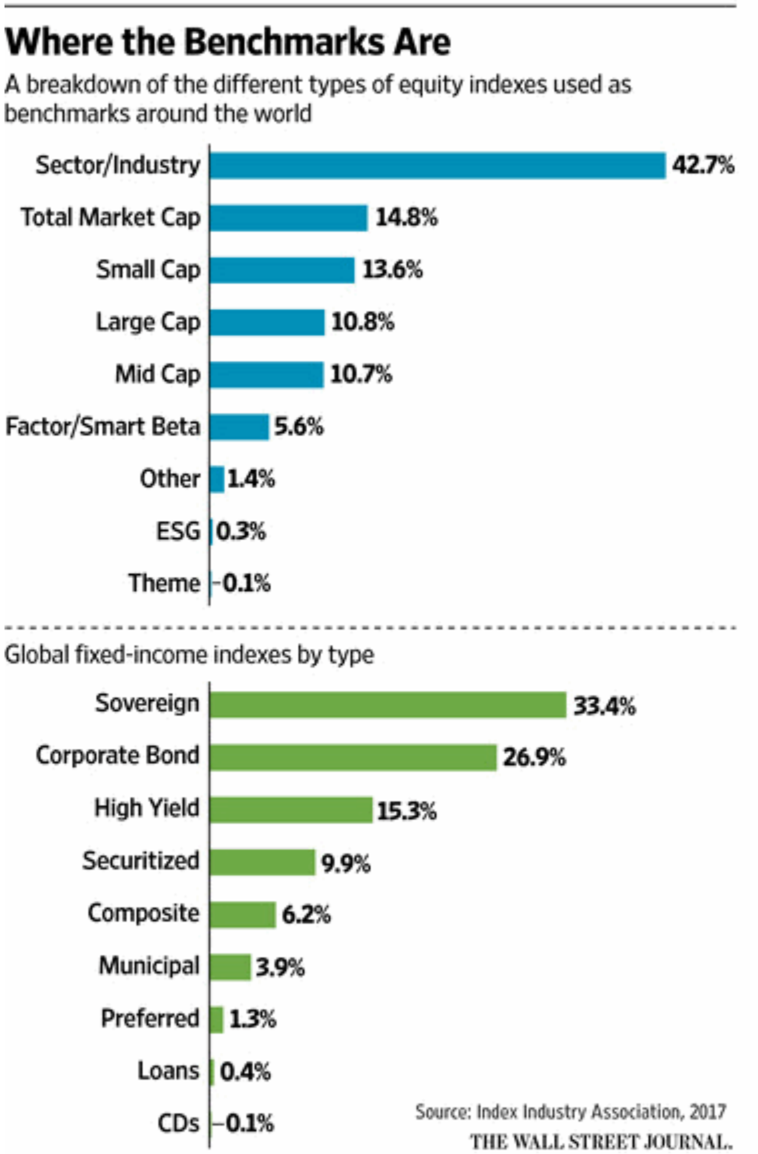
Thus, the personalized index fund is greeted with skepticism, even as industry watchers can't help but acknowledge its potential.

At a press briefing at the recent Morningstar Investment Conference in Chicago, Morningstar Chief Executive Kunal Kapoor said he believes that "the do-it-yourself crowd will go in that direction [of personalized funds], but the average investor probably won't take it that far."

But a moment later, he was asked what the next generation of investors is demanding from the financial-services industry, and his answer showed the potential of the personalized portfolio.

"Personalization is very big to the new generation," Mr. Kapoor said. "They want something tailored to them instead of being put into a black box. They want to know how their money is working for them. They want transparency and low costs. And those are all things they're going to insist on and won't be satisfied without."

Mr. Jaffe is a writer in Boston. He can be reached at reports@wsj.com.



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THE WALL STREET JOURNAL.
U.S. EDITION

Trade Spat Batters Global Markets

By Akane Otani, Mike Bird and Shen Hong
916 words
20 June 2018
The Wall Street Journal
J
B1
English

Global stocks, commodities and bond yields tumbled Tuesday, the starkest sign yet of investors betting tensions between the U.S. and China could escalate into a trade war.

Stocks had slid on trade worries repeatedly this year, only to bounce back as investors wagered the Trump administration's rhetoric would prove more posturing than actual policy. The scale of the market's pullback Tuesday exposed the vulnerability of those bets: showing investors reassessing their appetite for risk after doubting the willingness of the world's two largest economies to pursue policies that could cause long-lasting economic damage.

The **Dow Jones Industrial Average** tumbled 1.1%, or 287.26 points, for its biggest one-day slide of the month, while the Shanghai Composite Index fell to its lowest level since mid-2016 and major indexes in Germany and France lost more than 1% apiece.

"Since the middle of 2016, we've all known this administration would take a harder line on trade, but I think for many of us the assumption was perhaps that the tough talk was just going to be a negotiating position," said Ron Temple, head of U.S. equities and co-head of multiasset investing at Lazard Asset Management. "Now, what's unnerving is that the trade dispute has broadened out well beyond China."

Analysts and investors said there is still room for a compromise. But rising trade tensions come as optimism about the outlook for world-wide economic growth is waning and political risk is perceived to be rising once again around the globe.

Economic data have softened in Europe and China while economists have remained relatively **bullish** about U.S. growth. The Federal Reserve Bank of Atlanta in May bumped up its forecast for second-quarter gross domestic product to 4.7%, retail sales surged last month and consumer spending continues to tick higher. But many now fear that those expecting a reconciliation between the U.S. and China could find themselves caught off guard.

A first round of U.S. tariffs is due to be implemented on July 6, and there is likely to be additional **volatility** in debt, equity and commodities markets between now and then, analysts said.

"We think the risk of a trade war is becoming much higher at this stage. In particular, the risk of misjudgment on both sides looks high," said Haibin Zhu, chief China economist at JPMorgan Chase.

The latest retrenchment in the markets took place after President Donald Trump called Monday for his administration to identify $200 billion in Chinese goods for a fresh round of tariffs, upping the ante after he had approved tariffs on $50 billion of goods Friday. Chinese officials have pledged to impose tariffs on hundreds of U.S. goods, something investors worry could dent profits, especially among U.S. auto makers, farmers and industrial firms.

Shares of industrial heavyweights that investors fear could take a hit under tighter trade policies tumbled, with Caterpillar Inc., Boeing Inc. and Deere & Co. losing more than 3% apiece.

Commodities prices also were stung, with soybean prices sliding 2.2% to their lowest level in more than two years on Tuesday and front-month copper for June delivery falling 1.8% for its fourth consecutive loss.

The trade tensions also pressured the Chinese yuan: It was down 0.3% against the U.S. dollar in offshore trading late Tuesday in New York, hovering around the lowest level since January.

"It's mainly the trade war that has created such panic in the market because the latest developments have surpassed the expectations of many people in China," said Zhang Gang, senior analyst at Central China Securities.

Some investors still hold out hope that Mr. Trump's latest call to expand tariffs will shape up to be more of a bargaining tool than a move toward cutting off trade relations altogether.

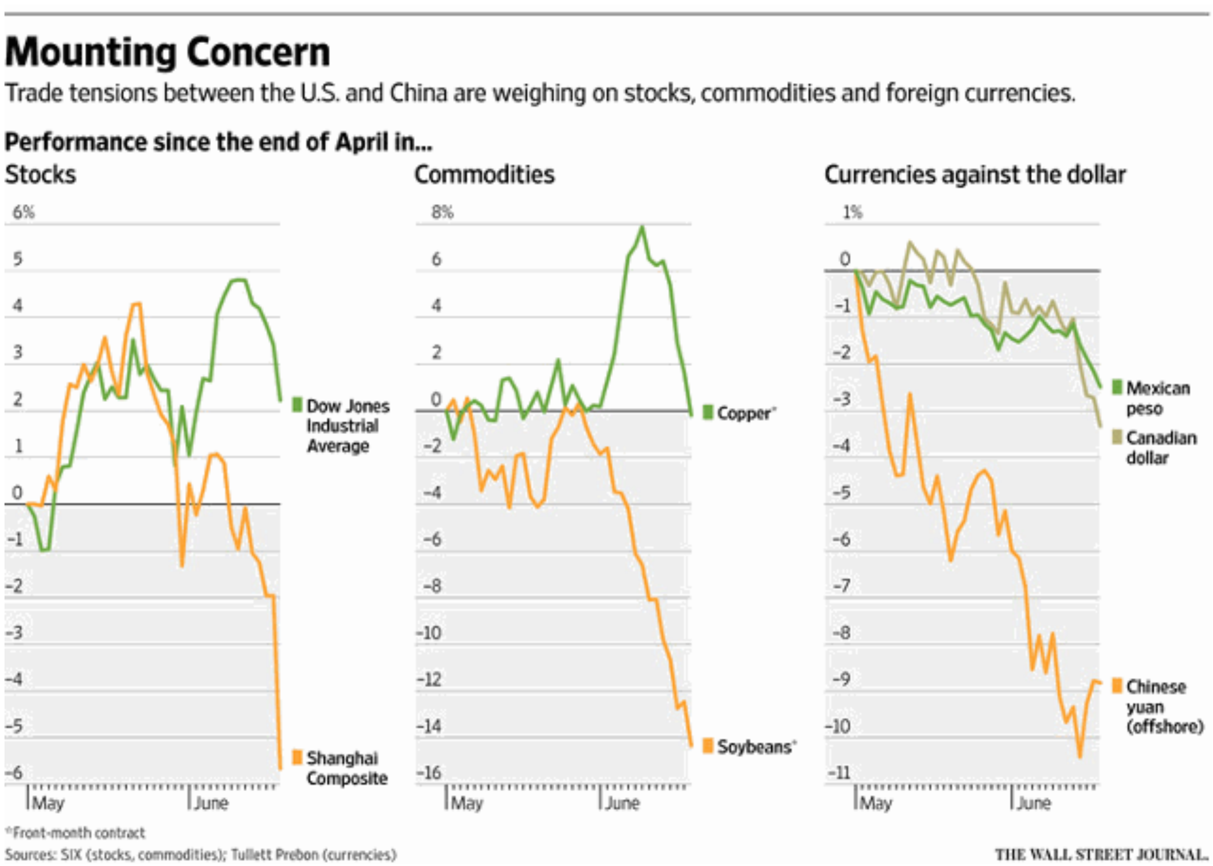
James Bianco, head of Chicago-based advisory firm Bianco Research, last week described the conflict between the U.S. and China as "watching sausage being made": a "nasty and ugly" process. Mr. Bianco said Tuesday that after the latest volley of threats between the U.S. and China, that appeared true "more so than ever."

For now, the White House is convinced it holds the upper hand and can eventually force China to concede and agree to better trade terms, Mr. Bianco said. It is a strategy that he thinks can work. "We've noticed that when Trump uses this blunt instrument, the power of the U.S., he gets what he wants," he said, adding he believes recent market action indicates that most investors have kept their cool.

Yet others are less optimistic, warning that the rise in trade tensions comes at a particularly inopportune time. The outlook for global growth has softened in recent months, while the dollar has appreciated, which some investors fear could send further ripples through indebted emerging-market economies.

The risk of policies being put in place that dent the global economy has risen over the past week, said Craig Birk, executive vice president of portfolio management at Personal Capital. "As threats increase and deadlines draw nearer, it increases the chances of miscalculation."

The selloff was more muted in Asia early Wednesday. The Shanghai Composite was down 0.4%, the Shenzhen Composite was down 0.3% and Japan's Nikkei Stock Average was down 0.3%.



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THE WALL STREET JOURNAL.
U.S. EDITION

Heard on the Street
Stock Investors Lower Their Aim

By Justin Lahart
485 words
20 June 2018
The Wall Street Journal
J
B14
English

[Financial Analysis and Commentary]

Volatility has returned with a vengeance. Tuesday was no exception, with stocks down sharply on renewed worries about President Donald Trump's trade feud with China. Yet for all the excitement, prices are back where they were in early January. Investors should be pleased to have gotten off so easily.

Stocks have some things going for them right now, of course. Corporate tax cuts boosted profits. Analysts polled by FactSet estimate second-quarter earnings for companies in the **S&P 500** will be up by 19% from a year earlier. Economic growth appears to have picked up, too.

But investors had already priced much of that in. What they hadn't anticipated were other risks. Chief among them are a Federal Reserve that is showing little timidity about raising rates, slowing growth overseas and the multiple trade skirmishes.

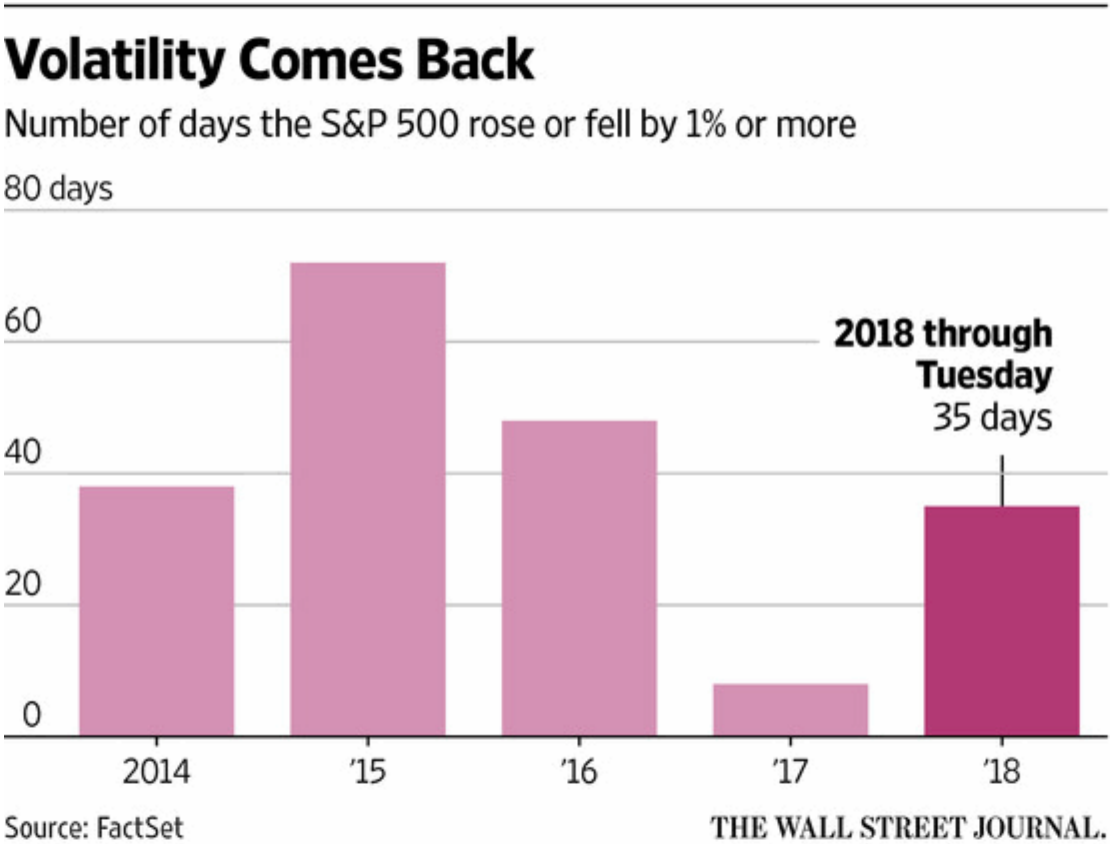
The Fed has raised rates by a quarter point twice already this year and policy makers are leaning toward raising them two more times in 2018. Futures markets now put the chances of two more increases at 51%. Compare that with the start of the year when the chances of four total rate increases were estimated at just 10%.

And with faster inflation and unemployment on course to drop from an already low 3.8%, the Fed will likely to have to keep lifting rates in 2019. That has helped push the yield on the **10**-**year Treasury** note to 2.88% from 2.41%. It might be higher still if it weren't for something else: Economists' growth forecasts for most other major economies have fallen since the start of the year. That makes for slower global demand growth at U.S. multinationals' overseas operations. Compounding the problem, stronger relative growth in the U.S. has boosted the dollar, lowering the dollar value of the goods and services that U.S. companies sell abroad.

One particular area of economic concern is China, which in the past countered weakening global growth with stimulus. Now it is reining in risky funding practices and damping its own growth as a result. Meanwhile, China's leaders are showing no sign of taking Mr. Trump's actions lying down. How that might affect U.S. companies is a wild card.

The trade troubles, along with the Fed's moves and weaker global outlook, have led investors to lower their expectations. The **S&P 500** now trades at 16.6 times expected earnings, according to FactSet, versus 18.2 times at the start of the year. That compares with a five-year average of 16.2, yet those were five years in which interest rates were significantly lower.

The **stock market**'s ability to absorb body blows therefore looks more limited at a time when the punches keep on coming.



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THE WALL STREET JOURNAL.
U.S. EDITION

World News: Trade Fight Softens China Debt Control --- Dispute with U.S. tests campaign to rein in business lending as wider economy slows

By Lingling Wei
748 words
20 June 2018
The Wall Street Journal
J
A6
English

BEIJING -- A bruising trade fight with the U.S. comes at a difficult time for China as its economy faces headwinds that limit President Xi Jinping's options.

While Chinese officials have been bracing for a trade war for months -- promising to match the Trump administration measure for measure -- there are signs China's recent economic expansion is slowing, from weakening investment and household consumption to rising corporate defaults, in part due to a key Xi initiative to contain debt and fend off financial risks.

The slowdown is triggering mounting calls from some corners of the government for Beijing to reopen the credit spigot and ease off on Mr. Xi's program before the trade conflict further dents growth.

"It's a testing moment for Beijing," said Larry Hu, China economist at Macquarie Group, a Sydney-based investment bank.

Soaring levels of corporate and local-government debt are seen by economists as potentially dragging down the world's second-largest economy. Getting a handle on debt has been a Xi priority.

The Trump administration's simultaneous fights with the European Union, Canada, Mexico, Japan and others on trade do give Beijing some breathing room, making it less likely that those U.S. allies will mount a broad front against Chinese trade practices widely seen as unfair. They also give the Chinese leadership a chance to pick up potential partners against Washington.

The latest volley from President Donald Trump, who said Monday that he had directed aides to identify $200 billion of Chinese goods for 10% tariffs, caught Beijing off guard. Officials scrambled to put together a strongly worded response, pledging to fight back forcefully without providing details.

By escalating the tariff threats to potentially $200 billion of Chinese goods, the Trump administration is, in effect, driving Beijing to look for penalties other than tariffs; the U.S. exports about $150 billion in goods to China.

Beijing could restrict access to China's market by American companies, tie up firms already there in antitrust and other regulatory red tape, and try to steer business to other foreign firms. The Trump administration already accuses Beijing of unfair practices, so targeting American business would reinforce that perception, likely hardening the response.

Early Tuesday, hours after the Trump announcement on additional tariffs, the People's Bank of China pumped 200 billion yuan, or $31 billion, of one-year funds into the nation's banks.

Advisers to the central bank said the move didn't mean the bank was loosening its conservative monetary stance, but was aimed at calming jittery investors and containing any financial fallout from the trade fight.

Still, the unusually large liquidity injection surprised market participants, helping drive down the yuan's value against the dollar to its weakest level in five months, at 6.4743. The benchmark Shanghai Composite **stock index** plunged 3.8% Tuesday, falling below 3000, a psychologically important level for investors and hitting its lowest mark in two years.

To fend off an economic slowdown, some officials in the State Council, China's cabinet, are urging more aggressive loosening measures to boost lending and spur growth, such as reducing the portion of deposits banks are required to hold in reserve. Others, notably those at the central bank and other financial regulators, want to stay the course of debt control.

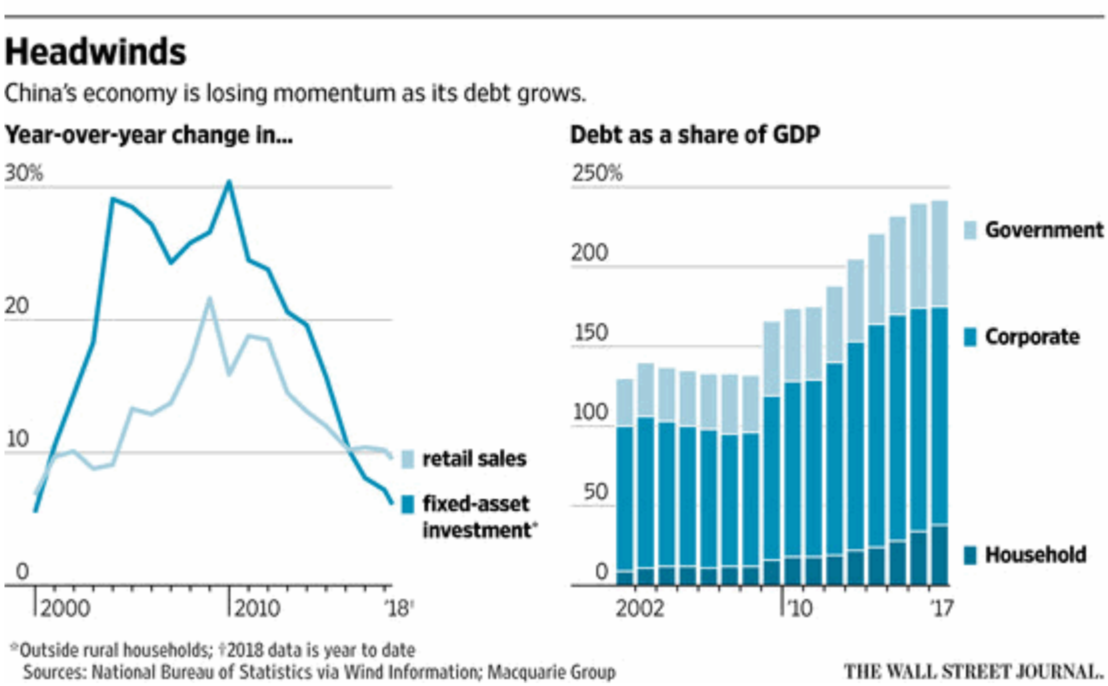
"Financial deleveraging is now trickling down to the real economy," said Sheng Songcheng, a senior adviser at China's central bank. "All those efforts would go to waste if monetary policy gets loosened now."

How China adjusts its economic policy, officials and economists said, will depend on how much worse the trade fight with the U.S. becomes.

Recent snapshots of economic activity show that investments in Chinese factories and other fixed assets have slowed to the lowest level in 18 years and China's household consumption, which has been steady in recent years, is starting to decelerate sharply.

With exports likely to take a hit too, policy makers have put in place tax cuts and other measures aimed at boosting consumption. Deutsche Bank AG estimates that an escalation of the conflict to include $200 billion of Chinese exports would shave between 0.2 and 0.3 percentage point from China's annual gross-domestic-product growth.

Chao Deng contributed to this article.



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THE WALL STREET JOURNAL.

World
The 10-Point. A personal, guided tour to the best scoops and stories every day in The Wall Street Journal.

By Matt Murray
1,052 words
20 June 2018
06:31 AM
The Wall Street Journal Online
WSJO
English

Good morning,

Tariff Trouble

President Trump's escalation of trade threats against China reflects his belief that Washington increasingly has the upper hand in the dispute, administration officials said. Mr. Trump caught Chinese officials off guard with his announcement Monday evening about potential new tariffs. Should China retaliate against U.S. trade policies, the White House said, the U.S. would apply tariffs of 10% on as much as $400 billion in Chinese imports. China had earlier threatened to retaliate against the U.S.'s initial round of 25% tariffs on $50 billion of imports announced last week. The White House proposal to apply a new round of tariffs would certainly hit many consumer products, from appliances to clothing to electronics, if enacted. The prospect of a trade war roiled global markets Tuesday, though stocks around the world regained ground Wednesday.

Migrant Morass

President Trump urged House Republicans to pass broad immigration legislation in a Tuesday evening meeting, but he stopped short of telling them he would reverse a widely condemned policy that has separated thousands of migrant children from their parents. In the private meeting, Mr. Trump discussed taxes, tariffs and the Russia probe before endorsing two different Republican immigration bills, according to lawmakers in the room. The meeting set the stage for House Republican leaders to begin lining up votes for a compromise bill that is seen as having the best chance of passing later this week. But the president's performance did little to give momentum to bills that are tentatively set for votes on Thursday, because he didn't line up behind one and sell it.

Dow Dropout

General Electric will drop out of the Dow industrials next week, a milestone in the decline of a company that once ranked among the mightiest of blue chips and was a pillar of the U.S. economy. It will be replaced by drugstore retailer Walgreens Boots Alliance, the latest sign of the rise of the global consumer economy and the postcrisis boom in debt issuance that has fueled a global deal-making frenzy. The decision to drop GE, an original member of the Dow that has been a part of the 30-**stock index** continuously since 1907, marks the latest setback for a conglomerate that once was the most valuable U.S. company, but has been hit hard in recent years by the unraveling of its finance business and competitive problems. GE shares have tumbled 55% over the past 52 weeks, erasing more than $100 billion in wealth.

Tequila Rising

When actor George Clooney and model-turned-entrepreneur Rande Gerber's tequila company, Casamigos, sold for $1 billion last year, it raised the question: How did the once-humble swill become so swank? A trek through Mexico distills all. Once the rotgut demon choice of hung over spring-breakers and hell-raisers, tequila has been elevated to, as the Mexican Chamber of the Tequila Industry literature trumpets about its annual festival, "Regalo de Mexico para el mundo," Mexico's gift to the world. Buyouts, including Bacardi acquiring tequila giant Patrón in a deal valued at $5 billion, are merely part of tequila's raging **bull market**.

Today's Video

At Odds

Turkey's President Recep Tayyip Erdogan's increasing authoritarianism and pursuit of a nationalist agenda have put his country at odds with its U.S. and NATO allies. Meanwhile, he's found a friend in Vladimir Putin.

TOP STORIES

U.S.

U.S. Withdrawing From U.N. Human Rights Council

Cohen Called In Loan While Seeking Funds to Pay Stormy Daniels

WORLD

Gaza Strip Militants Fire Rockets Into Israel

Saudi Employers Pursue Elusive Saudi Workers

BUSINESS

Ford and Volkswagen Discuss Developing Vehicles Together

McKinsey Investments Weren't Disclosed in Bankruptcy Cases

MARKETS

Cryptocurrency Exchange Bithumb Loses More Than $30 Million in Hack

Icahn Wins Majority on SandRidge Board

Number of the Day

$1.6 billion

The amount AT&T is expected to pay if it acquires AppNexus. The telecom giant is in talks to acquire the advertising technology company, the Journal reports.

Today's Question

Going back to our story above, what are your thoughts on General Electric being dropped from the Dow industrials? Send your comments, which we may edit before publication, to 10point@wsj.com. Please include your name and location.

—Compiled by Jessica Menton

Reader Response

Responding to yesterday's question on President Trump's threatening new tariffs on $200 billion in Chinese goods, Catherine England of Virginia said: "This will not end well for the U.S. Lost in the news about the trade deficit is the fact that the U.S. is the second-largest exporter in the world. Upping the stakes with additional tariffs will reduce foreign sales for our exporters and increase domestic prices at home while alienating former allies." Jack Palmer of Colorado shared: "Trump is looking out for Americans. He's doing what he was hired to do. The Chinese have never been good trading partners. They have always played the import-export game to their advantage and now they are being called [out] on it. Glad to see it." Richard Spaulding of New Jersey weighed in: "In the end, we will pay more for goods. There goes our so-called savings from tax breaks!" And Harry Howell of North Carolina wrote: "The U.S. standing up to China's unfair trade practices is long overdue....The present administration is to be commended for standing up for American industry, the American worker and ultimately the solvency of our country. Equalizing tariffs is the only language that the Chinese government understands."

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

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

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Economy

Undoing Negative Rates | Bullard: Central Banks Flattened Phillips Curve | Risk of Chinese Devaluation | What to Watch in Stress Tests | Blackstone's Take: Swiss Confront ECB Signals; The Wall Street Journal's central banking newsletter for Wednesday, June 20, 2018

2,087 words
20 June 2018
05:42 AM
WSJ Pro Central Banking
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English

Blackstone's Take: Swiss Confront Complicated Signals from ECB

Countries Face the Tricky Task of Undoing Negative Interest Rates

Bullard: Inflation-Fighting Measures by Central Banks Have Flattened Phillips Curve

What to Watch in the Fed's Stress Tests

Risk of Chinese Currency Devaluation Rises With Latest Tariffs Threat

Swiss Confront Complicated Signals from ECB

Mixed messages from the European Central Bank must be making heads spin in Switzerland.

Last week, the ECB signaled that it would likely end its bond-buying program at the end of year. That is good news for Switzerland, which needs the ECB to take the lead in normalizing its monetary policy before the Swiss National Bank can follow suit.

But the ECB also said it wouldn't raise its minus 0.4% deposit rate before September 2019. And ECB President Mario Draghi seemed to hedge a bit on the December bond wind-down on Tuesday, saying it "is subject to incoming data confirming the medium-term inflation outlook."

What does it mean for the SNB's rate decision Thursday? Not much. The SNB is widely expected to keep its deposit rate at minus 0.75% and signal a continued willingness to intervene in currency markets if it feels the Swiss franc is too strong.

But these mixed signals matter greatly for later this year and 2019, not just for Switzerland but for other non-euro central banks in Europe, including Denmark and Sweden.

Because these economies are so sensitive to trade with the eurozone and, thus, their exchange rates against the euro, they are unlikely to move aggressively on rates before the ECB starts tightening policy. That complicates the already difficult task of lifting negative interest rates.

In a cautionary sign for the SNB, the euro weakened about 0.4% against the Swiss franc after Mr. Draghi's comments Tuesday.

The question for the SNB and its non-euro peers is whether they have to wait for the ECB to raise rates before following suit. On that point, economists seem divided.

As long as the euro-franc rate is above 1.10 next year, the SNB can raise its deposit rate in the first quarter of next year independently of what the ECB does, say analysts at Credit Suisse.

In contrast, HSBC has moved back its forecast for the first SNB rate increase from the third quarter of 2019 to December next year.

Whatever the precise timing, the ECB will likely have to give a clear signal that rate increases are imminent before the Swiss can proceed with their own policy normalization.

Key Developments Around the World

Countries Face the Tricky Task of Undoing Negative Interest Rates

Europe has finally emerged from its debt crisis with healthy economic growth, but it can't shake one relic of its troubled times: negative interest rates. The policy was tried by Sweden briefly in 2009 and 2010 but eventually was implemented by Denmark, the eurozone, Switzerland and Sweden again over the subsequent five years before landing in Japan two years ago. Negative rates helped safeguard economic recoveries by lowering borrowing costs across fixed-income markets and, in some cases, boosting exports via weaker exchange rates. None of these economies seems willing to be the first to lift rates above zero for fear of derailing their recoveries. But the longer the banks wait, the greater the risk that damaging side effects—such as squeezing bank profits or fueling housing bubbles—may materialize.

Bullard: Inflation-Fighting Measures by Central Banks Have Flattened Phillips Curve

Central bankers have gotten so good at containing inflation over the past 30 years that they have obscured the link between inflation and unemployment, Federal Reserve Bank of St. Louis President James Bullard said Tuesday. In a presentation in Portugal, Mr. Bullard said central banks reacted so strongly and effectively to bring down inflation in the 1970s and 1980s that inflation has since become less **volatile**. That means periods of low unemployment are unlikely to push it up, he said. "Ultimately, successful monetary policy can push the empirical Phillips curve slope all the way to zero," he said. The relationship between inflation and unemployment, known as the Phillips curve, underlies much of central banking's economic analysis. The idea is that when unemployment falls below a certain level, it will trigger wage gains and price increases.

Dallas Fed Flags Global Under-Supply of Oil in Coming Years

Oil pricescould rise more in the years ahead as global supply begins to lag behind ever-growing demand, but a strong U.S. economy should be able to handle the higher prices, the Federal Reserve Bank of Dallas said in a report released Tuesday. "Historically, recessions in the U.S. have often followed **oil price** shocks," said the report, written by Dallas Fed President Robert Kaplan. "Higher **oil prices** tend to increase costs to consumers, which can, in turn, reduce their disposable income and consumption of non-oil goods and services." But the surge of domestically produced oil from shale has the U.S. now producing about 11 million barrels a day of crude oil, double the rate from 2011. This has created tens of thousands of new jobs in drilling, oil-field services, trucking, shipping and other sectors, and that "means that a larger share of the economy is helped by higher **oil prices**," the report said.

Transcript: Media Q&A With Atlanta Fed's Raphael Bostic in Savannah

Federal Reserve Bank of Atlanta President Raphael Bostic answered reporters' questions after speaking at a Rotary Club of Savannah event in Georgia on Monday. He talked about his outlook for interest rates, the flattening of the yield curve in the bond market and Federal Reserve Chairman Jerome Powell's decision to hold a press conference after every policy meeting. Here is a transcript of the exchange.

Don't Fight the Fed's Balance Sheet Taper

The Federal Reserve's move to trim the size of its bondholdings has exacerbated recent declines in prices for risky assets around the world, investors say. The central bank has scaled back its mountain of Treasury and mortgage debt by $111.9 billion since the policy was announced in September. More than half the reduction has taken place since the end of March, and the process of withdrawing money from the economy is scheduled to reach $50 billion a month in October.

New Bank Regulator Sets 'Open Door' Policy on Rule Changes

The new leader of a key U.S. bank regulator said her agency needs to be more responsive to the industry's concerns and wants to review how regulators enforce "living will" requirements for big banks. Federal Deposit Insurance Corp. Chairman Jelena McWilliams, in her first public remarks since being sworn in less than two weeks ago, avoided staking out specific policy positions but declared that her agency has an "open door policy where we solicit feedback on what's working and what's not" in the U.S. bank rule book.

What to Watch in the Fed's Stress Tests

Stress-test season kicks off with the first round of results on Thursday. The Federal Reserve is reviewing the health of the nation's largest banks and their ability to withstand crisis-like situations, such as a spiking unemployment rates or other adverse economic conditions. Next Wednesday, the Fed will release the second, more consequential, round of results. A pass or fail in that round will determine whether a bank can increase dividends or share buybacks.Here are four things to watch as the Fed prepares to deliver its first stress-test results under Trump-appointed officials.

Risk of Chinese Currency Devaluation Rises With Latest Tariffs Threat

The Trump administration's threat to place tariffs on another $200 billion in Chinese goods has reignited fears that Beijing will turn to a powerful but risky weapon: a depreciation of its currency. The latest salvo in the brewing trade conflict between the world's first and second-largest economies would raise the amount of Chinese goods taxed by the U.S. to $450 billion. That would mean tariffs on nearly all of the $505 billion in goods that China exported to the U.S. last year. Analysts say the tariff escalation could eventually lead China to depreciate its currency, the yuan—a maneuver that would help to offset the economic impact of the tariffs but also threatens to worsen trade tensions and rattle global markets.

Trade Fight With U.S. Complicates China's Campaign to Contain Debt

A bruising trade fight with the U.S. lands at a difficult time for China as its economy contends with rising headwinds, constraining Chinese President Xi Jinping's options. While Chinese officials have been bracing for a trade war for months—promising to match the Trump administration measure for measure—signs are rising that China's recent economic expansion is ebbing, from weakening investment and household consumption to increasing corporate defaults, in part due to a key Xi initiative to contain debt and fend off financial risks.

Philippines Central Bank Raises Benchmark Rates

The Philippine central bankraised its benchmark interest rates, as widely expected, with the inflation rate running above its target. Bangko Sentral ng Pilipinas lifted its overnight borrowing rate to 3.50% from 3.25% and its overnight lending rate to 4.00% from 3.75%, effective Thursday. That marked the second increase this year, after rates were raised in May.

Quick Hits: Riksbank's Negative Rate Policy Could Backfire, SEB Says

Sweden's negative interest rate policy is seen as potentially leading to an "inflation problem," the eurozone's current-account surplus eased further in April, and comments from China's central bank could point to further policy easing. Here are quick hits on central banking and related market views from around the world.

Wednesday

Time N/A

Central Bank of Brazil releases policy statement

9:30 a.m. EDT

Fed's Powell, ECB's Draghi and Bank of Japan's Kuroda speak

10 a.m. EDT

National Association of Realtors releases May U.S. existing-home sales

9:30 p.m. EDT

Bank of Japan's Funo speaks

Thursday

Time N/A

Federal Reserve releases industrywide stress test results

Time N/A

Bangko Sentral ng Pilipinas releases policy statement

Time N/A

Bank of Mexico releases policy statement

3:30 a.m. EDT

Swiss National Bank releases policy statement

4 a.m. EDT

Norges Bank releases policy statement

7 a.m. EDT

Bank of England releases policy statement and minutes

8:45 a.m. EDT

ECB's Nouy speaks in Amsterdam

9 a.m. EDT

Minneapolis Fed's Kashkari speaks

4:15 p.m. EDT

Bank of England's Carney speaks

The Impact of Non-Tariff Barriers on EU Goods Trade After Brexit

"Time-sensitive goods are found to be most at risk of suffering from increases in non-tariff barriers" to European Union exports to the U.K. after Brexit, Stephen Byrne and Jonathan Rice find in a VoxEU column. "Based on current trade composition, Latvia, Ireland, and Denmark are the trading partners that will be most affected," they write.

The Other Yield Curve Investors Should Watch as Trouble Mounts

"Escalating trade tensions have helped push the **U**.**S**. **Treasuryyield** curve to its flattest in more than a decade. This flattening is watched closely by investors as an indicator of economic trouble ahead. But another curve deserves attention too—and it is getting steeper," writes Richard Barley for The Wall Street Journal. "That is the corporate-bond spread curve, which measures how much extra compensation investors are demanding to take credit risk at different time horizons," Mr. Barley says.

U.S. housing starts rebounded last month to the highest level since 2007, driven by a construction rebound in parts of the country that have lagged behind for much of the economic recovery as well as a lingering apartment boom.

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THE WALL STREET JOURNAL.

Markets

Several Asian Countries, Including China, Are Dangerously Close to Bear-Market Territory; Trade tensions worry global investors, but several regional markets are the hardest hit

By Steven Russolillo
577 words
20 June 2018
12:02 AM
The Wall Street Journal Online
WSJO
English

Markets in China and Hong Kong flip flopped between gains and losses Wednesday after suffering steep declines in the previous session prompted by fears of a full-blown trade war between Washington and Beijing. Other major regional markets fared better, as Korea's Kospi index rose 1% and Japan's Nikkei 225 index gained 0.2%.

Wednesday's Big Theme

China is one of several countries in Asia approaching **bear-market** territory.

What's Happening

Trade tensions have spooked investors globally, but several markets in Asia have been hit the hardest.

China's benchmark index, the Shanghai Composite, has fallen 19% from its high in January. That puts it on the verge of a new **bear market**, widely considered to be a drop of at least 20% from a recent high.

Markets in the Philippines and Indonesia are down 19% and 14%, respectively, from highs earlier this year. Vietnam, which had risen 22% through early April and was the biggest gainer in Asia Pacific, lost it all nearly two months later and fell into a new **bear market**. It is currently down about 20% from that high.

By comparison, the **S&P 500** is up for the year and sits just 4% away from its all-time high. In Europe, the Stoxx Europe 600 is off 5% from its year's high.

The recent decline in China—by far Asia's biggest market—comes after President Donald Trump's escalated trade threats. It also comes after a prolonged stretch of low **volatility** that was partly driven by government intervention intended to keep markets calm. China hasn't been in a **bear market** since the summer crash of 2015, when stocks plunged nearly 50% in a couple of months.

The recent selloff comes at an inopportune time for a company like Xiaomi Corp., the Chinese smartphone giant that is aiming for an initial public offering in the coming weeks. The company this week postponed a plan to conduct a large portion of its IPO in Shanghai. That move came just days after it had submitted paperwork to issue those Chinese securities.

Xiaomi said Tuesday that it will launch these so-called Chinese Depositary Receipts "at an appropriate time" after the company lists in Hong Kong.

Market Reaction

"At this point, the tariffs are not yet a game changer, but risks are increasing," said Keith Lerner, managing director at SunTrust Advisory Services.

"One can understand if U.S. trading partners are getting frustrated, added Mike O'Rourke, chief market strategist at U.S. brokerage firm JonesTrading. "If the Trump administration's decisions to actively continue to escalate trade tensions is not enough, injury is added to insult due to the fact that foreign **financial markets** are succumbing to the burden."

Louis Kujis, head of Asia economics at Oxford Economics, said that "In principle, there is still room for negotiation and we cannot rule out de-escalation in the coming weeks. But attitudes seem to be hardening.

"Deeper conflicts are also hard to resolve," he added. "Indeed, it looks like the probability of a full-blown trade war between the world's two largest economies is rising."

Elsewhere

U.S. Treasury yields fell slightly and the U.S. dollar was steady.

Write to Steven Russolillo at steven.russolillo@wsj.com

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The New York Times

Foreign Desk; SECTA
U.S. Threats Stir Worries Of Slowdown

By MATT PHILLIPS and PRASHANT S. RAO; Elsie Chen contributed research from Beijing.
557 words
20 June 2018
The New York Times
NYTF
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8
English

Wall Street's focus returned on Tuesday to a fast escalating trade war and the damage it could do to business confidence and economic growth. Global stock benchmarks and commodity prices fell.

The trigger for the drop was the statement by President Trump on Monday that his administration was prepared to impose tariffs on a further $200 billion of Chinese goods, and that there could be even more penalties if Beijing fought back. The United States and China have already announced plans for tit-for-tat tariffs on $50 billion worth of imports each.

With the latest threat from Mr. Trump, the White House is warning that it could impose trade restrictions on as much as $450 billion of imports from China, a figure that is nearly equivalent to the total value of goods that China sold to the United States last year.

On Tuesday, a spokesman for the Chinese Foreign Ministry, Geng Shuang, said the United States was "abandoning all the consensus that has been achieved, changing its mind constantly."

Across **financial markets**, it appears that investors are starting to take seriously how such a trade conflict could become a drag on a global economy that's expected to grow at a relatively strong 3.9 percent in 2018, according to International Monetary Fund forecasts.

In the United States, the **Dow Jones Index**, the **Standard & Poor's 500-stockindex** and the tech-heavy **Nasdaq composite** all fell on Tuesday. The Dow's drop of 1.2 percent was its worst day this month, and pushed it into slightly negative territory for the year.

Industrial companies including Caterpillar and Boeing weighed heavily on the benchmarks, dropping more than 3 percent each.

The trading followed declines in stock markets in Frankfurt, London and Paris. Shares in Hong Kong, Tokyo and mainland China also closed sharply lower.

Investors moved their money into haven assets like 10-year United States Treasury bonds and the Japanese yen. The yield on the benchmark **10-year Treasury** note, which moves in the opposite direction of its price, fell below 2.90 percent early Tuesday, in a sign that at least some investors were concerned about risks to growth.

In the markets for commodities, the raw materials on which the global economy runs, the declines were widespread. Copper, a barometer for industrial activity, was down, as was crude oil.

Some of the sharpest drops were in the agricultural commodities markets, where the price for soybeans -- a politically sensitive crop given Mr. Trump's support among farmers -- plunged early Tuesday before stabilizing. China, the world's largest importer of soybeans and the largest buyer of American soybeans, has threatened to levy tariffs on American exports as part of the growing trade hostilities.

The reaction of global markets underscores the fact that the dispute between China and the United States is part of a broader protectionist drive by the Trump administration that has already disrupted global trade.

"Most damaging for businesses and investment," analysts at the Swiss bank UBS said in a report on Tuesday, "is perhaps rising uncertainty caused by lasting trade disputes, which could delay or significantly change business and investment decisions."

Follow Prashant S. Rao on Twitter: @prashantrao.

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The New York Times

Foreign Desk; SECTA
Global Markets Slump on Fears Of a Trade War

By ANA SWANSON; Alan Rappeport contributed reporting from Washington, Prashant S. Rao from London, and Matt Phillips from New York.
1,720 words
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English

WASHINGTON -- President Trump's threat to impose tariffs on almost every Chinese product that comes into the United States intensified the possibility of a damaging trade war, sending stock markets tumbling on Tuesday and drawing a rebuke from retailers, tech companies and manufacturers.

The Trump administration remained unmoved by those concerns, with a top trade adviser, Peter Navarro, insisting that China has more to lose from a trade fight than the United States. He also declared that Mr. Trump would not allow Beijing to simply buy its way out of an economic dispute by promising to import more American goods.

''President Trump has given China every chance to change its aggressive behavior,'' Mr. Navarro said in a call with reporters on Tuesday. ''China does have much more to lose than we do.''

In threatening tariffs on as much as $450 billion worth of Chinese goods, the administration is betting that Beijing will blink first. It's a risky gamble by a White House that appears ready to forgo diplomatic negotiations in favor of punishing tariffs that could pinch consumers and companies on both sides of the Pacific.

The approach fulfills a frequent campaign promise by Mr. Trump. But it has spooked companies, investors and markets, which are increasingly worried that the United States has no other strategy to resolve a stalemate with China over its trade practices. Several rounds of trade talks with top Chinese officials in Washington and Beijing produced little agreement, and no additional official negotiations are scheduled, administration officials said.

On Tuesday, Mr. Trump suggested he was ready for a fight, saying China would no longer take advantage of the United States.

''China has been taking out $500 billion a year out of our country and rebuilding China,'' the president said during a speech in Washington before the National Federation of Independent Business. ''They've taken so much. It's time folks, it's time. So we're going to get smart, and we're going to do it right.''

Markets sank on Tuesday in response to Mr. Trump's announcement late Monday that his administration was preparing to impose even more tariffs than he originally threatened if China continued with its plan to retaliate against the United States.

Mr. Trump is now threatening to tax nearly the total value of goods that China sent to the United States last year, which was $505.6 billion.

The benchmark **Dow Jonesindex**, the **Standard & Poor**'**s 500**-**stockindex** and the tech-heavy **Nasdaq composite** all fell on Tuesday, following stock markets in Frankfurt, London, Paris, Hong Kong, Tokyo and mainland China. Investors moved money into assets that are considered safe havens, like 10-year United States Treasury bonds and the Japanese yen.

Shares of Boeing and Caterpillar, which are among America's leading exporters to China, fell sharply on Tuesday, along with soybean futures. China is the world's largest importer of soybeans, a key livestock feed, and Beijing has targeted American soybeans for retaliation with its own tariffs.

Soybean prices dropped more than 7 percent at times during the morning before stabilizing in afternoon trading. Prices are at their lowest level in more than two years, creating a politically delicate issue for Mr. Trump, who has strong support from rural voters in farm states but whose trade policies have angered farmers and lawmakers who represent them.

Senator Joni Ernst, an Iowa Republican, said in a statement, "These aggressive trade actions will continue to have damaging consequences, including an impact on our commodity prices and farm futures, and increasing anxiety among the agricultural and business communities in Iowa."

But Mr. Navarro, who is among Mr. Trump's most strident anti-China advisers, dismissed those concerns, saying the United States had no choice. He said that the White House had given China numerous opportunities to negotiate and alter policies that have cost Americans millions of jobs, and that the Trump administration was now prepared to impose tariffs on $450 billion of Chinese goods in order to force Beijing to bend.

"I think that the other side may have underestimated the strong resolve of President Donald J. Trump," Mr. Navarro said. "If they thought that they could buy us off cheap with a few extra products and allow them to continue to steal our intellectual property and crown jewels, that was a miscalculation. We hope going forward there are no more miscalculations."

Mr. Navarro said a trade clash would hurt China much more than the United States, given that the value of China's exports to the United States was nearly four times the value of what the United States exports to China.

For weeks, the United States and China had appeared close to a deal that would have forestalled tariffs. Top advisers like Steven Mnuchin, the Treasury secretary, and Wilbur Ross, the commerce secretary, had advocated a deal that could avoid the devastating effects of a trade war, and spent hours in negotiations with Chinese officials.

But after the Chinese refused to commit to a target for reducing their trade surplus with the United States or limit industrial subsidies, Mr. Trump rejected those proposals. And his resolve only hardened after lawmakers, including Democrats, criticized him as being weak on China when he agreed to help ease penalties on ZTE, a Chinese telecommunications company accused of violating American sanctions.

That decision has triggered a huge fight between the White House and Congress. On Monday, the Senate passed legislation that would reinstate penalties on ZTE and rescind a Commerce Department deal that allowed the company to stay in business in exchange for paying a large fine and agreeing to a series of management and compliance changes. The White House has vowed to remove that provision before the bill becomes final, and Mr. Trump is expected to meet with lawmakers on Wednesday to discuss the fate of ZTE.

The president's approach has irritated some of Mr. Trump's own advisers, including Mr. Mnuchin, who has been frustrated by the process of the China talks, according to an official familiar with his thinking. Mr. Mnuchin has tried to explain in recent meetings how China is likely to respond to America's threats and the impact that retaliation could have on **financial markets** and the economy.

He has also been trying to persuade Mr. Trump not to proceed with harsh restrictions on Chinese investment that would limit China's ability to do business in the United States. The Treasury Department is expected to release a proposal this month. Mr. Mnuchin, who is leading the effort, has been trying to convince Mr. Trump that the restrictions are unnecessary, given pending legislation that would expand national security reviews performed by the Committee on Foreign Investment in the United States.

In late May, Mr. Mnuchin helped orchestrate a meeting between the president, top White House advisers and Republican lawmakers, where the Treasury secretary asked lawmakers to help make the case that legislation would be a more targeted way to police Chinese investment, three people with knowledge of the meeting said. But Mr. Navarro and Robert E. Lighthizer, the United States trade representative, who were also in the meeting, objected to that approach. The president ultimately overruled Mr. Mnuchin, saying that he supported the congressional legislation but that it alone wasn't enough.

The decision to proceed with tariffs is a victory for hard-liners in the administration, like Mr. Navarro and Mr. Lighthizer. They had argued that the United States should not back down from trying to force China to make more fundamental changes to its economy, even if such measures would cause short-term pain for American businesses and consumers.

On Tuesday, Mr. Navarro minimized the divisions between administration officials, saying the United States' negotiating process had not wavered and was "linear." He said the idea of dropping the trade case in exchange for purchases -- something the Chinese had offered the Americans in negotiations -- had always been a "nonstarter."

In his remarks Tuesday morning, Mr. Navarro took aim at China's internal plan to develop cutting-edge industries like robotics, new-energy vehicles, advanced rail and shipping, and aerospace. He said the country could not be allowed to dominate technologies that would be an important source of jobs and growth for the United States in decades to come.

China has engaged in unfair practices, including cybertheft and "information harvesting," to obtain technological secrets from the United States that would allow China to pull ahead in these industries, Mr. Navarro said.

"It is important to note here that the actions President Trump has taken are purely defensive in nature," he said.

There is broad agreement that China has engaged in unfair trade practices that have hurt American companies. But Mr. Trump's resort to tariffs as his primary negotiating tool has prompted swift condemnation from retail, technology and manufacturing companies, who said the approach could hurt American consumers and companies more than the White House realized.

Jose Castaneda, spokesman for the Information Technology Industry Council, called the escalation of trade tensions with China "irresponsible and counterproductive."

"We appreciate President Trump's efforts to protect the United States' 'crown jewels,' but tariffs are simply the wrong way to do it," he said. "The White House needs to work with our allies to create lasting change with China. Too many jobs and livelihoods are at stake to get this wrong."

Matt Priest, the president of the Footwear Distributors and Retailers of America, said it was difficult to see how tariffs on an additional $200 billion of Chinese goods wouldn't "negatively impact all Americans of every walk of life."

"The president claimed that trade wars are easy to win, but what our industry has always known is coming true: Trade wars are costly, unnecessary and do harm to the American economy," he said.

Follow Ana Swanson on Twitter: AnaSwanson.

A batch of iPal robots on exhibit in Shanghai last week. In 2017, China sent $505.6 billion in goods to the United States.; Soybeans in Nantong, China, in April. Beijing has threatened tariffs on American soybean imports. (PHOTOGRAPHS BY AGENCE FRANCE-PRESSE -- GETTY IMAGES) (A8)

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THE WALL STREET JOURNAL.

Business

Is Bitcoin the Future, or an Echo of a Failed Past? Digital currencies remind some of the spread of private money in the early 19th century

By Paul Vigna
1,085 words
19 June 2018
10:28 PM
The Wall Street Journal Online
WSJO
English

For most of its 10-year history, the digital currency bitcoin has been viewed by some people as the future of money.

Lately, to get some insight into what the future might hold, some are focusing on how bitcoin compares with currencies of the past.

In the early days of the United States, before the dollar was king, most paper money was issued not by the federal government, but by private banks. That system fell out of favor after the Civil War, as the government asserted its role in currency management.

The cryptocurrency revolution that started during the global financial crisis has started to change perceptions, giving new credence to the idea that private money could complement, or in some cases replace, government currencies.

Not that anyone expects that to happen on a grand scale soon. Bitcoin's use as a currency is still more theoretical than actual, and other cryptocurrencies are even farther from the mainstream. Most of the activity around bitcoin and the others revolves around trading them, not buying things.

But there are some real-world uses for bitcoin. A smattering of small businesses accept it. Online travel sites Expedia and CheapAir.com accept it. In Japan, businesses like electronics retailer Yamada Denki accept it. There are even two Montessori Schools in New York City that accept bitcoin.

"The current situation could be described as a drift" back toward private money, said James Bullard, president of the Federal Reserve Bank of St. Louis, at a presentation for cryptocurrency investors in New York last month.

Study of the topic is growing more timely after last year's rally in bitcoin and other cryptocurrencies brought throngs of new investors to the sector. As of late May, more than 1,600 virtual currencies and coins had been launched, according to tracking site CoinMarketCap.

Lost faith

Private money usually proliferates when many people see a lack of credible alternatives. In the early 19th century, private money flourished as U.S. banks created their own currencies to meet demand in a rapidly expanding nation whose federal government was still relatively weak. In frontier encampments, lumber companies would issue company-backed "scrip." Oil and railroad companies issued their own money, too.

Today, the demand for cryptocurrencies is being driven partly by pure speculation, and partly by technological developments that make them a faster, cheaper alternative to official currencies for making payments. But there are more-dramatic factors at work as well: In countries that have suffered rampant inflation or other economic crises, some people have turned to private money as a more-reliable alternative to official currencies ravaged by the actions of their governments.

Indeed, bitcoin first appeared in late 2008, at the height of the global financial crisis, appealing to people who felt government institutions around the world were failing. "Clearly when people have any insecurity about government plans, they flock to other assets," says Emin Gün Sirer, an associate professor of computer science at Cornell University. Traditionally, gold has provided that perceived haven. Now, for many people, it's cryptocurrencies instead.

In other words, some people believe that technology and algorithms will do a better job of managing currencies than governments will.

Troubling echoes

The historical record, though, shows that private money tends to create as many problems as it solves.

In one way, bitcoin is a clear improvement over pre-Civil War private money: The amount of new money created is known in advance, programmed right into bitcoin's code, and the total number of bitcoins that can be created is capped at 21 million. The program also is designed to make counterfeiting impossible. In the 19th century, nobody knew exactly how much currency was in circulation, and counterfeiting was a nagging problem.

On the other hand, there are troubling similarities to the old days: All the new currencies popping up can create confusion and conditions ripe for fraud. While bitcoin has become more widely accepted, boosting its potential to become a viable international currency, its $130 billion market value now represents only about 40% of the overall cryptocurrency market's value, according to CoinMarketCap. About 700 new currencies have come out of nowhere in the past year alone. That proliferation has added to bitcoin's already **volatile** nature, making it difficult to put a value on the currency that even approaches the stability of the dollar and the world's other major currencies.

As Mr. Bullard described in his May 14 speech, in the 19th century, "the profusion of privately issued currency created an unsatisfactory system" in which users were frustrated by the chaos and unpredictability of **volatile** exchange rates. Moreover, mismanagement of their currencies led many of the issuing banks to collapse, rendering their currencies worthless.

Today, because there are so many cryptocurrencies, they "may unwittingly be pushing in the wrong direction in trying to solve an important social problem," said Mr. Bullard.

A real-life lesson

Users of bitcoin have seen both the benefits and the pitfalls. Tunga, a Kampala, Uganda-based staffing service that connects freelance tech developers in Africa with companies around the world, started experimenting with bitcoin in 2015 because it found dealing in traditional currencies across borders too slow and expensive.

The firm started using a bitcoin-based payments network in 2015. Initially, its freelancers were getting paid in minutes rather than days, and because of that speed and the relative stability of bitcoin's value at the time, fluctuating exchange rates weren't a problem, says Bart Leijssenaar, Tunga's chief marketing officer.

That changed in 2017, though. Bitcoin's price spiked, then started falling back to earth. The network couldn't handle the increased traffic smoothly. Suddenly, transactions were taking much longer to settle, and the value of payments was becoming subject to bitcoin's **volatile** exchange rates.

Eventually, Tunga returned to more-traditional currencies. "The potential is very big," Mr. Leijssenaar says of bitcoin, "but it has to be stable for this to really work."

Mr. Vigna is a Wall Street Journal reporter in New York. He can be reached at paul.vigna@wsj.com.

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THE WALL STREET JOURNAL.
U.S. EDITION

U.S. News: Housing Starts Reach Their Highest Level Since 2007

By Laura Kusisto
474 words
20 June 2018
The Wall Street Journal
J
A3
English

U.S. housing starts rebounded last month to the highest level since 2007, driven by a construction rebound in parts of the country that have lagged behind for much of the economic recovery as well as a lingering apartment boom.

Housing starts rose 5% in May from the prior month to a seasonally adjusted annual rate of 1.35 million, the Commerce Department said Tuesday. Compared with a year earlier, starts were up 20.3%.

The strong improvement was spread fairly evenly between single-family and multifamily, despite expectations that builders would pull back on new apartment construction because of a flood of new units already hitting the market. Single-family construction increased 3.9% in May, compared with a month earlier, while multifamily building increased 11.3%, according to the Commerce Department.

Midwestern builders also significantly ramped up construction, welcome news for a region that had lagged behind compared with the South and the West through much of the economic recovery.

Wells Fargo & Co. Senior Economist Mark Vitner said part of the bump in the Midwest may be attributable to an improving manufacturing sector. "The economic recovery has broadened and it's reached parts of the country that hadn't seen improvement until recently," he said.

Housing-starts data are **volatile** from month to month and can be subject to large revisions. May's 5% jump for starts came with a margin of error of plus or minus 10.2 percentage points.

Building permits, which tend to be a more reliable indicator and signal how much construction is in the pipeline, declined 4.6% to an annual pace of 1.301 million last month. Permit declines in the South and West drove May's permits figure lower. Permits last month fell for both single-family and multifamily housing.

Nonetheless, housing construction appears on track to have a slightly better year than many economists had predicted, in part, because of surprisingly strong multifamily growth.

Overall starts grew by 11% in the first five months of 2018, compared with the same period a year earlier. Multifamily starts rose 13.3% during that period; single-family starts rose 9.8%.

Still, builders face headwinds in the coming months. Rising lumber prices have added nearly $9,000 to the cost of a new home since January 2017, according to the National Association of Home Builders, which reported on Monday that builder confidence ticked down slightly in June.

Mr. Vitner said larger home builders have more power to negotiate deals on material and labor prices, but smaller builders are struggling. "A lot of smaller builders are having to postpone projects . . . and say let's just sit this out and see if prices come down," he said.

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White House Sees Edge in China Talks

By Bob Davis and Lingling Wei
1,120 words
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English

President Donald Trump's escalation of trade threats against China reflects his belief that Washington increasingly has the upper hand in the dispute, administration officials said, adding he is prepared to withstand pressure from U.S. businesses that might suffer from the conflict.

Mr. Trump caught Chinese officials off guard with his announcement Monday evening about potential new tariffs. Should China retaliate against U.S. trade policies, the White House said, the U.S. would apply tariffs of 10% on as much as $400 billion in Chinese imports. China had earlier threatened to retaliate against the U.S.'s initial round of 25% tariffs on $50 billion on imports announced last week. The bulk of those tariffs go into effect July 6.

News of the new tariffs and the prospect of a trade war roiled global markets Tuesday. The **Dow Jones Industrial Average** fell 1.1% and the Shanghai Composite Index dropped 3.8% to its lowest level since mid-2016. Indexes in major exporters Germany and France slid more than 1%. Commodities prices also took a hit, with soybean prices dropping 2.2% to their lowest level in more than two years.

The White House's tough stance represents the ascendancy, for now, of trade hawks in the administration, particularly White House senior trade adviser Peter Navarro and U.S. trade representative Robert Lighthizer. Both officials argue China represents a fundamental threat to the U.S. that needs to be countered, even at the cost of pain to the U.S. economy.

"It's clear that China has much more to lose" than the U.S. from a trade fight, said Mr. Navarro.

Mr. Lighthizer said additional tariffs wouldn't be imposed until the U.S. picked the products, and received industry comment, a process that will take months and leaves open the possibility of additional negotiations. But so far there is no indication that such talks are on the horizon, and the administration is signaling that it is increasingly confident of achieving goals through a dramatically more confrontational approach to China.

Although Chinese government officials pledged to fight back forcefully, they didn't give any details of what they might do, as they have in the past. Beijing has threatened to match the initial U.S. tariffs dollar-for-dollar and impose them on the same day as the U.S. acts.

Next up from the administration is a plan to halt Chinese investment in U.S. technology, due to be released by the Treasury Department by June 30. Under the plan, which is still being developed, the U.S. would use a law designed to address national emergencies to block Beijing from acquiring what the White House calls "industrially significant technology." Export controls on such technologies would also be tightened, say administration officials.

Mr. Trump has backed away from threats before, and sided with advisers who take a less confrontational attitude toward China, including Treasury Secretary Steven Mnuchin. In April, Mr. Trump threatened a dramatic increase in tariffs on Chinese goods, but didn't follow through. Instead, he approved negotiations Mr. Mnuchin led to get China to buy more U.S. goods and make changes to its tariffs and other trade barriers. That led to a temporary reprieve in the tensions as the two sides sought to negotiate a truce.

The White House has since judged those efforts a failure, especially after Mr. Mnuchin and Mr. Trump were criticized by cable TV hosts and some lawmakers of being weak on China. During a June trade mission to China by Commerce Secretary Wilbur Ross, Beijing offered to buy nearly $70 billion in U.S. farm, manufacturing and energy products if the Trump administration abandoned tariff threats. Mr. Trump rejected that offer as another empty promise.

"The other side may have underestimated" if they thought the White House could be swayed by pledges of purchases, said Mr. Navarro. "That was a miscalculation."

The hard-liners in the Trump administration increasingly believe Beijing is vulnerable on trade because China exports far more merchandise to the U.S. -- $505.5 billion last year -- than the U.S. sends to China. In 2017, the U.S. exported goods worth $129.9 billion to China. Mr. Navarro said the U.S. goal is "enforceable, accountable, systematic change" in Chinese economic and trading practices.

Although global trade now accounts for less than one-third of China's gross domestic product, compared with nearly two-thirds in 2006, strong exports were a big reason why China's growth exceeded the government's target last year. A sharp slump in exports in the coming months, economists say, could threaten growth just as investments in Chinese factories and other fixed assets are slowing to multiyear lows, while Chinese household consumption is starting to weaken.

U.S. officials also note another vulnerability of their Chinese counterparts: While China imports less than the U.S., its economic growth is more dependent on what it does import, especially on the machinery and technology.

China has plenty of weapons it can employ to respond to the confrontational U.S. trade policies, including stepped-up regulations of American companies operating in China and stirred-up nationalist resentment.

Using Tariffs as a

Line of Defense

For Tech Companies

The White House says tariffs will protect U.S. technology from Chinese predation. Beijing obtains U.S. technology by stealing it, the White House alleges, and by forcing U.S. companies in China to transfer technology to Chinese firms.

Administration officials say tariffs will change incentives for foreign firms and prompt them to move manufacturing operations from China. Even if they relocate elsewhere in Asia rather than the U.S., that, the officials argue, will hinder China's ability to acquire advanced technology.

Josh Kallmer, senior vice president at the Information Technology Industry Council, a trade association, says the administration's plans would hurt U.S. companies by driving up costs and making them uncompetitive.

The threatened tariffs "are notjust counterproductive, they are irresponsible," he said. "You can't just pick up a factory and move it to Vietnam. It takes years to move physical operations. It takes months to renegotiate contracts. It's not a practical solution."

Administration officials counter that U.S. firms adapt more quickly than they acknowledge. They argue that reducing Chinese influence over U.S. companies is worth the short-term pain. If U.S. companies are eventually able to operate in China without fear of government pressure, "this economy will be stronger, the global economy will be stronger," said White House senior trade adviser Peter Navarro.

-- Bob Davis

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GE Drops Out of the Dow After A Century

By Michael Wursthorn and Thomas Gryta
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English

General Electric Co. will drop out of the **Dow Jones Industrial Average** next week, a milestone in the decline of a firm that once ranked among the mightiest of blue-chips.

It will be replaced by drugstore retailer Walgreens Boots Alliance Inc., the latest sign of the rise of the global consumer economy and the postcrisis boom in debt issuance that has fueled a worldwide deal-making frenzy.

The decision to drop GE, an original member of the Dow that has been a part of the 30-**stock index** continuously since 1907, marks the latest setback for a company that once was the most valuable U.S. firm but has been hit hard in recent years by the unraveling of its finance business and competitive problems.

With the departure of GE and the addition of Walgreens, "the **DJIA** will be more representative of the consumer and health care sectors of the U.S. economy," said David Blitzer, chairman of the index committee at S&P Dow Jones Indices, the company behind the Dow. "Today's change to the **DJIA** will make the index a better measure of the economy and the **stock market**."

GE shares have tumbled 55% over the past 52 weeks, erasing more than $100 billion in wealth, as the company has switched leaders, slashed its dividend payment and pursued a restructuring that could result in a breakup of the struggling conglomerate. It is the cheapest stock of all 30 Dow components.

"We are focused on executing against the plan we've laid out to improve GE's performance," a GE spokeswoman said. "Today's announcement does nothing to change those commitments or our focus in creating in a stronger, simpler GE."

Shares of GE fell 1.4% in after hours trading. While investors don't expect the company's departure from the Dow to be a long-term drag on its share price, some said its exit was a potent symbol of how far the company's elevated status has fallen.

GE's market capitalization peaked at $594 billion in 2000, making it the most valued U.S. company. It has shrunk over the years. Under former CEO Jeff Immelt, the company shed its NBCUniversal media business and sold off most of its GE Capital arm.

More recently, the Boston-based company struck a deal to sell its century-old railroad business, part of a plan to shed $20 billion worth of assets by the end of next year. It is also looking to sell its century-old lighting business.

Investors are waiting for a major portfolio update from CEO John Flannery, who took over last summer and continues to preach that "everything is on the table." Mr. Flannery has also been slashing jobs and cutting costs as GE struggles with slack sales in its big Power business, which sells turbines for power plants.

GE's decline has left it with a market value of $113 billion, but it wasn't the smallest industrial in the venerable index. GE's market cap and annual revenue are still larger than Dow member United Technologies Corp.

Walgreens ended Tuesday's session with a market value of $64 billion.

Component stocks of the Dow are selected by the index committee, a group that includes editors of The Wall Street Journal, which is published by Dow Jones & Co., a part of News Corp.

The shake-up won't affect the value of the Dow, which fell 1.15% Tuesday and is down 0.1% this year. The index has surged to dozens of records in the past several years, most recently in January.

Akane Otani contributed to this article.

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Heard on the Street
The Other Yield Curve To Watch

By Richard Barley
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[Financial Analysis and Commentary]

Escalating trade tensions have helped push the **U**.**S**. **Treasuryyield** curve to its flattest in more than a decade. This flattening is watched closely by investors as an indicator of economic trouble ahead. But another curve deserves attention, too -- and it is getting steeper.

That is the corporate-bond spread curve, which measures how much extra compensation investors are demanding to take credit risk at different time horizons. The U.S. curve has steepened, as spreads versus Treasurys have widened more on long-maturity bonds than they have on short-maturity bonds.

Investors now get 1.7 percentage points more yield than Treasurys for corporate debt maturing in 10 years or more, versus 0.68 point for one-to-three-year debt, according to ICE BofAML indexes. Three months ago, the gap was roughly one-fifth tighter.

The message this sends is that while investors have become more uncertain about the longer-term outlook, they are relaxed about the near term.

For now, the credit curve seems likely to only get steeper, in particular because companies have issued a lot of risky long-dated debt. The size of the U.S. triple-B-rated 10-year-plus index has surged to $878 billion from $235 billion 10 years ago.

The danger point is a combination of wider credit spreads and a flatter credit curve, which would signal deeper concerns about company balance sheets. The good news is this isn't something corporate-bond investors are betting on -- yet.

page,5043

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THE WALL STREET JOURNAL.
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Politics & Ideas: The Perils of Corporate Concentration

By William A. Galston
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English

Amid the din of daily political combat, it's easy to overlook long-term trends reshaping the country. The **stock market** has quadrupled since 2009's Great Recession low, but the growth of real wages has failed to accelerate, even as unemployment has fallen from 10% to under 4%. An International Monetary Fund paper published earlier this month suggests these developments are linked to a single cause -- increasing corporate concentration throughout the U.S. economy.

A standard definition of market power, say the authors of the IMF paper, is the ability to maintain prices above marginal cost -- the level that would prevail under perfect competition. They find that between 1980 and 2016, markups by U.S. companies have increased by an average of 42%. Although markups have risen in all major industry sectors, some have experienced increases far above the average, led by 419% for biotechnology. Not surprisingly, there is a strong relationship between markups and profitability.

There is also evidence that markups are related to market concentration, which has surged in recent decades. Since the mid-1990s the standard measure of concentration used in antitrust analysis, the Herfindahl-Hirschman Index, has risen by 50%.

These findings have important real-world consequences, says the IMF. At first higher markups are associated with increasing investment in both physical plant and research and development. But beyond a certain point the relationship reverses. "At higher levels of markups, or at higher levels of market concentration," the authors find, "the marginal relation between innovation and markups becomes negative." In short, as a firm's market position strengthens, its incentive to invest in innovation decreases. If we care about the pace of innovation in the economy, we have reason to resist excessive levels of sectoral concentration.

There's another reason to care about companies' rising market power: as the level of concentration rises, the IMF paper concludes, firms can appropriate "a growing share of the rents from production," leaving less for labor. Unlike the relationship between concentration and innovation, which takes the shape of an inverted U that rises and then falls, the relationship between concentration and returns to labor is linear: The higher the market concentration, the lower the labor share.

Rising market concentration means more for profit and less for labor. This helps explain why wages have increased so slowly since the Great Recession even as the **stock market** has soared. If we have reasons to care about workers' ability to share in the growth of their firms -- and we do -- we have little choice but to rein in market concentration when it upsets the balance that makes the American dream possible.

This conclusion has nothing to do with a sentimental attachment to small business, let alone an ideological preference for individual producers. As modes of production change, so will the scale of production. Some technologies make smaller companies more profitable, while others push in the opposite direction. In the aggregate, technological change has made possible increased economies of scale, an evolution we have no compelling reason to resist.

"Too much of a good thing is wonderful," said Mae West. She was an acute social observer, but not much of an economist. If big is beautiful, it doesn't follow that bigger is even more beautiful. Beyond a certain point, which can only be determined empirically rather than theoretically, growing company size has perverse consequences. The practical question is whether we will accept these consequences as unavoidable or use public policy to resist them.

The time has come to reinvigorate antitrust enforcement. The current guidelines state: "Mergers that cause a significant increase in concentration and result in highly concentrated markets are presumed to be likely to enhance market power." Although this is the right principle, in practice regulators have adopted an excessively restrictive definition of what counts as a significant increase. This has led to a myopic focus on the most highly concentrated sectors -- those with four or fewer competitors -- even when somewhat less concentrated sectors also experience rising market power. The Justice Department and the Federal Trade Commission should adopt a broader view.

In addition, companies in concentrated sectors can engage in two different forms of anticompetitive behavior -- "exclusionary" conduct that prevents new competitors from entering a market, and "exploitative" conduct that allows dominant parties to take advantage of their market power. At present, U.S. regulators have few tools to address the latter abuse, forcing the government to rely on public shaming to counteract predatory pricing such as Mylan's notorious 400% price hikes for its EpiPen.

We can argue about the details, but without more effective measures to counteract hyperconcentration, American workers will continue to draw the short straw.

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THE WALL STREET JOURNAL.
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Fresh Push On Tariffs To Offer Test For Investors

By Ben Eisen
200 words
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The Trump administration's threat of fresh tariffs on Chinese goods is testing whether stock investors will continue to shrug off the risk of a more restrictive trade policy.

The **S&P 500** fell as much as 1.1% Tuesday after President Donald Trump asked his advisers to identify a list of $200 billion in Chinese exports that would face new penalties. The move followed the U.S.'s application of tariffs on $50 billion in imports from China last week, after which the Chinese government issued its own retaliatory tariffs. The S&P ended the day down 0.4%.

Trade threats have injected **volatility** into U.S. stock markets since the end of February.

Some investors see the most recent trade dispute as a potential turning point, given that the dollar amount of items potentially subject to new tariffs has grown, and China has vowed to retaliate.

"The market earlier in the year thought this was just a negotiating tactic. Now, it's becoming a bit more serious," said Liz Young, senior investment strategist at BNY Mellon Investment Management.

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THE WALL STREET JOURNAL.
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Investors Worry About Fate Of Nafta

By Ira Iosebashvili and Akane Otani
737 words
19 June 2018
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B11
English

Escalating trade tensions are rattling markets as a new round of tariffs raises investors' concerns about everything from U.S.-China relations to the fate of the North American Free Trade Agreement .

The mounting strains left investors struggling to understand the sweeping ramifications of those conflicts, including their impact on economies, interest rates, inflation and stock valuations. President Donald Trump approved tariffs on about $50 billion of Chinese goods on Friday, prompting Chinese officials to hit back with tariffs of their own.

The moves, which investors said exacerbated fears that the world's two biggest economies could descend into a full trade war, buffeted government-bond yields Friday and shares of agricultural and industrial companies that could suffer under tighter trade policies. Caterpillar Inc . slid 2% Friday, while farm-machinery maker Deere & Co . lost 1%, Boeing Co . fell 1.3% and U.S. Steel Corp . declined 4.2%. Declines in industrial heavyweights pulled the **Dow Jones Industrial Average** to its biggest one-week slide since March.

Now, investors are debating whether **financial markets** that had already been struggling for momentum this year will be able to shake off an increasingly uncertain outlook for global trade and growth.

While the U.S. economy continues to exhibit signs of strength, investors and analysts say they are concerned about the rise of restrictive trade policies because so much activity depends on cross-border transactions. The feud over Nafta poses a particularly acute manifestation of those fears. Mr. Trump, who has threatened to withdraw entirely from the accord, removed the U.S. from the Trans-Pacific Partnership as one of his first official acts in office.

The step "would be a strong signal to the global community that the U.S. is really embracing the America-first agenda," said Mark McCormick, North American head of FX strategy at TD Securities . "That's probably bad for globalization, bad for equities, bad for risk."

Any signs that the deal might be replaced with bilateral agreements between the U.S., Canada and Mexico would likely take the edges off market moves, analysts said. On the other hand, emerging-market currencies, commodities prices and Mexican and Canadian assets could slide if it appeared the Nafta conflict was the prelude to an all-out global trade war.

Many investors and analysts fear that a U.S. withdrawal from Nafta could further hamper a U.S. **stock market** that has struggled to gain ground this year, denting profits for companies that produce and export automobiles, agricultural goods -- including corn, soybean and beef -- and industrial machinery.

Through Nafta, U.S. car manufacturers such as Ford Motor Co . and General Motors Co . have been able to shift production to Mexico, where wages are typically lower. Some economists argue that without access to lower-cost production hubs, the U.S. auto industry could lose ground to competitors in Asia. The disruptions could also cause foreign car makers to rethink their investments in U.S. production facilities.

"These sort of linkages, which have given U.S. auto makers an advantage in relation to China, would be much more difficult without Nafta's tariff reductions and protections for intellectual property," a 2017 analysis by the Council on Foreign Relations said.

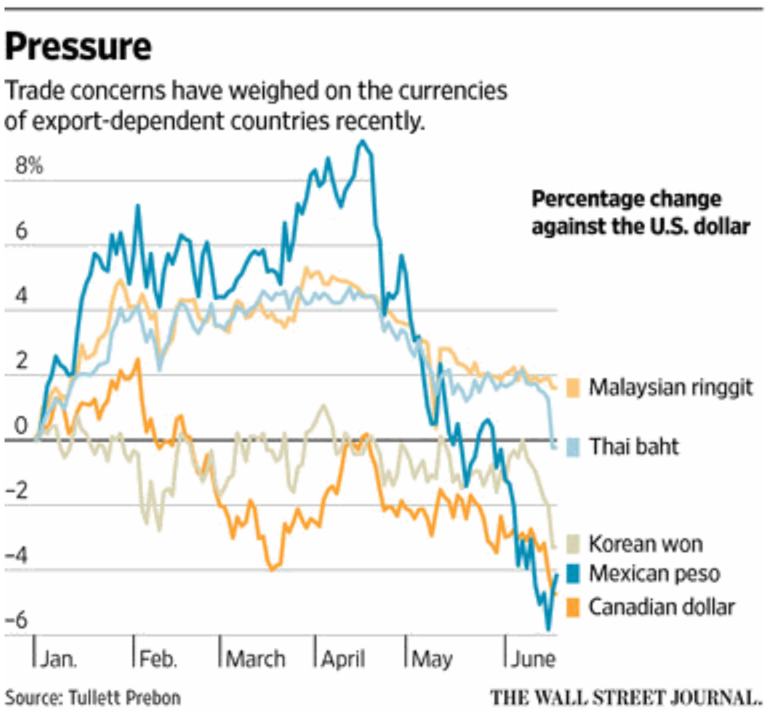
Shares of agricultural and industrial firms could also take a hit. The U.S. exported $43 billion of prepared food, vegetables, fruit and other food and beverages and $85 billion of machinery to Canada and Mexico last year, according to federal data. Withdrawal from Nafta could squeeze profit margins at companies such as

Constellation Brands Inc ., which brews Corona and Modelo beer in Mexico, as well as agricultural giants like Archer Daniels Midland Co .

More broadly, some fear a U.S. exit from Nafta could trigger tit-for-tat trade measures that weigh on an even wider range of industries.

"Even if it ended up being replaced with something better for the U.S., that would take time, which adds to uncertainty among investors," said Karyn Cavanaugh , senior market strategist at Voya Investment Management.

Uncertainty over Nafta has already taken a toll on Mexican and Canadian markets. Stocks in both countries have stagnated this year, along with the **S&P 500**, which remains below its record high hit in January. The Mexican peso is down 4.1% against the dollar this year, while Canada's dollar is off 4.8%.



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THE WALL STREET JOURNAL.

Opinion
The GOP's Trade Abdication; Trump escalates his tariff war as Senators shrink from a debate.

By The Editorial Board
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19 June 2018
07:10 PM
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English

Would Republicans in Congress stay mute if a President imposed income or sales taxes on U.S. industries on an arbitrary whim? We doubt it, so it's dispiriting to see Senate Republicans let Donald Trump impose tens of billions of dollars in border taxes without so much as a vote of protest.

That's the sad story as GOP Senators last week blocked a vote on Bob Corker's amendment to reclaim at least some of the power to impose tariffs that Congress has ceded to Presidents. Perhaps Mr. Trump took the silence as assent because he is escalating. On Monday he threatened tariffs on up to $450 billion in Chinese goods, and **financial markets** are finally losing their foolish complacency. Shares in exporters vulnerable to retaliation like Boeing and Caterpillar fell more than 3.6% Tuesday.

Mr. Corker's bipartisan measure would have required Congress to approve trade restrictions that Mr. Trump is imposing under Section 232 of the Trade Expansion Act of 1962. This is the law that lets a President impose more or less whatever tariffs he wants with an elastic definition of national security. Mr. Trump has used this open-ended authority to inflict his 25% tariff on steel and 10% on aluminum, and he's threatening a 25% levy on imported cars under the same law. His new China tariffs are based on a different legal rationale (Section 301).

"I would bet that 95 percent of the people on this side of the aisle support intellectually this amendment," Mr. Corker said on the floor with some acidity. "And a lot of them would vote for it if it came to a vote. But, no, no, no. 'Gosh, we might poke the bear' is the language I've been hearing in the hallways."

Mr. Corker is right that GOP leaders fear a Trump tweet in the middle of election season. Some of them are also griping in private that Mr. Corker has the luxury of bucking the President because he isn't running for re-election. But Mr. Corker's modest bill isn't the political threat to Republicans. The growing damage from Mr. Trump's trade war is.

By not allowing trade votes, Republicans are giving Mr. Trump free rein to impose tariffs that are doing substantial economic harm to many of their constituents. Farm state Senators deserve a chance to vote against tariffs that are spurring retaliation against U.S. agricultural exports of everything from pork to apples. So do Senators who represent U.S. manufacturers. The fear of a Trump tantrum is precluding an important fight about what the party of free enterprise supposedly believes.

The economic fallout may also hurt the GOP's chances of holding the Senate in November. Democrats Heidi Heitkamp (North Dakota) and Claire McCaskill (Missouri) are running against the tariffs as a way to oppose Mr. Trump and defend their states' agricultural interests. The longer Republicans shrink from standing up to Mr. Trump's protectionism, the more voters will conclude that Republicans in Congress are complicit in the damage.

Foreign Edition Podcast

* Foreign Edition podcast: Angela Merkel's immigration battle.

Document WSJO000020180619ee6j007y5

The New York Times

Business/Financial Desk; SECTB

Trump Raises Stakes in Trade Conflict With a $200 Billion Threat

By ANA SWANSON, KEITH BRADSHER and KATIE ROGERS
1,508 words
19 June 2018
The New York Times
NYTF
Late Edition - Final
1
English

WASHINGTON -- President Trump further escalated his trade fight with China on Monday, saying his administration was prepared to impose tariffs on another $200 billion worth of Chinese goods and potentially even more if Beijing continues to fight back.

Mr. Trump's threat, in response to retaliatory measures by China, was the latest volley in a dizzying trade dispute that has pitted the world's two largest economies against each other and resulted in a seemingly endless game of one-upsmanship. The president called it punishment for what he said was an attempt by Beijing to keep the United States ''at a permanent and unfair disadvantage.''

''China apparently has no intention of changing its unfair practices related to the acquisition of American intellectual property and technology,'' Mr. Trump said in a statement. ''Rather than altering those practices, it is now threatening United States companies, workers, and farmers who have done nothing wrong,'' he added, calling China's response ''unacceptable.''

The president left little doubt that the United States would continue to hit back even harder if China counters, adding another tariffs to another $200 billion worth of Chinese goods. All told, the Trump administration is threatening to impose tariffs on as much as $450 billion worth of goods, including an earlier round -- a sum nearly as large as the total value of goods China sent the United States last year, which was $505.6 billion.

''The administration is essentially saying it is willing to bring a substantial amount of commercial activity in the Asia-Pacific to a screeching halt,'' said Scott Kennedy , a China expert at the Center for Strategic and International Studies .

The tit for tat began on Friday, when Mr. Trump said Washington would move ahead with tariffs on $50 billion worth of Chinese goods, including agricultural and industrial machinery. The action provoked an immediate response from Beijing, which said it would place its own tariffs on $50 billion worth of American goods, including beef, poultry, tobacco and cars.

On Monday, Mr. Trump raised the ante even further, saying that he had directed Robert E. Lighthizer , the United States trade representative, to pursue another $200 billion worth of tariffs.

China's Commerce Ministry responded swiftly to Mr. Trump's threat, issuing a statement on its website that warned that if the Trump administration followed through, China would ''have to adopt comprehensive measures combining quantity and quality to make a strong countermeasure.''

The rapid succession of trade threats has left little time for negotiations that could potentially defuse tensions between the two countries.

Whether President Xi Jinping of China agrees to bend to Mr. Trump's demands remains an open question. With his latest move, Mr. Trump has escalated his trade threats to such a level that China can now no longer issue a proportional response. Last year, the United States exported only $130.4 billion of goods to China in total.

But trade experts say there are plenty of ways beyond tariffs that the Chinese government could retaliate -- including slowing approvals for acquisitions made by American companies or stalling products at its ports. And Mr. Trump's aggressive challenges may have left the Chinese president with little room to back down without looking weak to his own population.

"Mr. Trump seems to be counting on the fact that China will soon run out of room to retaliate with its own tariffs on U.S. exports," said Eswar Prasad , a trade expert at Cornell University . "This could prove to be a miscalculation since China has other effective levers it can use in a trade war, including disruptions of American businesses' sales operations and their supply chains that run through China."

The White House imposed the tariffs as punishment for what the administration said was years of unfair trade practices by the Chinese government, including pressuring American companies to hand over valuable trade secrets in order to operate in that country.

Mr. Trump has been betting that the tariff threats will satisfy his supporters, who cheered his tough-on-China statements on the campaign trail. But China's retaliation could come back to bite some groups, especially American farmers, who are bearing the brunt of China's tariffs. And it is generating opposition within his own party among business-friendly Republicans who favor free trade and are increasingly concerned about Mr. Trump's approach.

Lawmakers of both parties have criticized the president's trade threats, but few have advocated taking direct action against him. Last week, Senate Republicans blocked a vote on legislation introduced by Senator Bob Corker , a Tennessee Republican, which would have given Congress the ability to overturn certain tariffs. Senate leaders said such a bill would have simply been vetoed by the president.

The trade conflict with China comes as the administration wages several trade conflicts at once. Rather than forming a coalition of countries to pressure China to change its trade practices, as some foreign leaders and trade officials have urged, the president has put allies on edge with tariffs on metal from Europe, Canada and Mexico and threats to withdraw from the North American Free Trade Agreement .

If they do go into effect, the tariffs would greatly increase the disruption for international companies, which are already anxious about the prospect of higher costs on many goods that move between the United States and China.

Kip Eideberg, the vice president of public affairs and advocacy at the Association of Equipment Manufacturers, which represents major American exporters like Caterpillar and John Deere, said the additional tariffs were "terrible news" for his industry.

"It will effectively wipe out all of the gains that our industry has seen from tax reform and regulatory relief," he said. "We should be creating more jobs, not wiping them out."

The Trump administration had said it intended its initial list of tariffs on $50 billion of Chinese products to have as little impact as possible on American consumers who purchase Chinese-made televisions, clothes and electronics. But ratcheting up the level of tariffs would eventually start to pinch consumers.

The tariffs could also damage investor confidence, potentially setting off **stock market** falls or persuading companies to withhold from investing in new facilities and factories. Already there are signs of strains in the global economy from the broader trade tensions, weakness that China and the United States are both better positioned to weather than other nations.

However, there's a chance Mr. Trump's tariffs may have a limited impact on China's nearly $13 trillion economy, which no longer depends as much on exports and can find other places besides the United States to sell its products.

Some American buyers of Chinese goods may simply choose to pay the newly imposed tariffs rather than find new suppliers elsewhere. Brad Setser , a Treasury official in the Obama administration who is now an economist at the Council on Foreign Relations , said that China's exports to the United States in the listed categories could easily be halved by the tariffs. But they would not disappear entirely, as some Chinese products would still be competitive in terms of cost.

Some of the same goods could probably be sold to other countries at slightly lower prices, further limiting the effect on the Chinese economy, Mr. Setser said. Moreover, China's exports could grow in other areas to offset any drop.

The tariffs could have a longer-term effect on China, however.

Devised as essentially a pre-emptive strike against China's enormous program to bolster high-tech industries, the Trump tariffs could limit eventual sales from China's emerging technologies. With the European Union also protesting the program called Made in China 2025, exports to Europe could suffer, too.

For both sides, the issue has become far more than a struggle over nuts-and-bolts economics. It has become a battle over which country will dominate the high-wage, high-skill industries of tomorrow. Washington and Beijing alike see those industries as essential to protecting national security and to creating jobs.

The Trump administration is pushing hard for curbs on the Made in China 2025 program. Beijing aims to make the country a leader in the manufacturing of advanced products, including computer microchips and commercial aircraft. The Trump administration's statement announcing tariffs managed to mention the Chinese industrial policy program no fewer than five times.

But China appears just as determined to preserve the program. And the trade issue has become so prominent that the Chinese public has come to expect that Beijing will push back hard against the Trump administration's trade measures.

''This pressure will be high,'' said Tu Xinquan, the director of the China Institute of World Trade Organization Studies in Beijing. ''There is no way to move back.''

There is a chance that the tariffs may have a limited impact on China's economy, which no longer depends as much on exports. (PHOTOGRAPH BY WILLIAM HONG/REUTERS) (B4)

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The New York Times

U.S.; Politics
Trump Threatens Tariffs on $200 Billion in China Goods, Escalating Fight

By Ana Swanson, Keith Bradsher and Katie Rogers
1,516 words
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WASHINGTON — President Trump further escalated his trade fight with China on Monday, saying his administration was prepared to impose tariffs on another $200 billion worth of Chinese goods and potentially even more if Beijing continues to fight back.

Mr. Trump's threat, in response to retaliatory measures by China, was the latest volley in a dizzying trade dispute that has pitted the world's two largest economies against each other and resulted in a seemingly endless game of one-upsmanship. The president called it punishment for what he said was an attempt by Beijing to keep the United States "at a permanent and unfair disadvantage."

"China apparently has no intention of changing its unfair practices related to the acquisition of American intellectual property and technology," Mr. Trump said in a statement. "Rather than altering those practices, it is now threatening United States companies, workers, and farmers who have done nothing wrong," he added, calling China's response "unacceptable."

The president left little doubt that the United States would continue to hit back even harder if China counters, adding tariffs to another $200 billion worth of Chinese goods. All told, the Trump administration is threatening to impose tariffs on as much as $450 billion worth of goods, including an earlier round — a sum nearly as large as the total value of goods China sent the United States last year , which was $505.6 billion.

"The administration is essentially saying it is willing to bring a substantial amount of commercial activity in the Asia-Pacific to a screeching halt," said Scott Kennedy , a China expert at the Center for Strategic and International Studies .

The tit for tat began on Friday, when Mr. Trump said Washington would move ahead with tariffs on $50 billion worth of Chinese goods, including agricultural and industrial machinery. The action provoked an immediate response from Beijing, which said it would place its own tariffs on $50 billion worth of American goods, including beef, poultry, tobacco and cars.

On Monday, Mr. Trump raised the ante even further, saying that he had directed Robert E. Lighthizer , the United States trade representative, to pursue another $200 billion worth of tariffs.

China's Commerce Ministry responded swiftly to Mr. Trump's threat, issuing a statement on its website that warned that if the Trump administration followed through, China would "have to adopt comprehensive measures combining quantity and quality to make a strong countermeasure."

[Read about Apple chief executive Tim Cook's efforts to keep his company from becoming collateral damage in a trade war.]

The rapid succession of trade threats has left little time for negotiations that could potentially defuse tensions between the two countries.

Whether President Xi Jinping of China agrees to bend to Mr. Trump's demands remains an open question. With his latest move, Mr. Trump has escalated his trade threats to such a level that China can now no longer issue a proportional response. Last year, the United States exported only $130.4 billion of goods to China in total.

But trade experts say there are plenty of ways beyond tariffs that the Chinese government could retaliate — including slowing approvals for acquisitions made by American companies or stalling products at its ports. And

Mr. Trump's aggressive challenges may have left the Chinese president with little room to back down without looking weak to his own population.

"Mr. Trump seems to be counting on the fact that China will soon run out of room to retaliate with its own tariffs on U.S. exports," said Eswar Prasad , a trade expert at Cornell University . "This could prove to be a miscalculation since China has other effective levers it can use in a trade war, including disruptions of American businesses' sales operations and their supply chains that run through China."

The White House imposed the tariffs as punishment for what the administration said was years of unfair trade practices by the Chinese government, including pressuring American companies to hand over valuable trade secrets in order to operate in that country.

Mr. Trump has been betting that the tariff threats will satisfy his supporters, who cheered his tough-on-China statements on the campaign trail. But China's retaliation could come back to bite some groups, especially American farmers, who are bearing the brunt of China's tariffs. And it is generating opposition within his own party among business-friendly Republicans who favor free trade and are increasingly concerned about Mr. Trump's approach.

Lawmakers of both parties have criticized the president's trade threats, but few have advocated taking direct action against him. Last week, Senate Republicans blocked a vote on legislation introduced by Senator Bob Corker , a Tennessee Republican, which would have given Congress the ability to overturn certain tariffs. Senate leaders said such a bill would have simply been vetoed by the president.

The trade conflict with China comes as the administration wages several trade conflicts at once. Rather than forming a coalition of countries to pressure China to change its trade practices, as some foreign leaders and trade officials have urged, the president has put allies on edge with tariffs on metal from Europe, Canada and Mexico and threats to withdraw from the North American Free Trade Agreement .

If they do go into effect, the tariffs would greatly increase the disruption for international companies, which are already anxious about the prospect of higher costs on many goods that move between the United States and China.

Kip Eideberg, the vice president of public affairs and advocacy at the Association of Equipment Manufacturers, which represents major American exporters like Caterpillar and John Deere, said the additional tariffs were "terrible news" for his industry.

"It will effectively wipe out all of the gains that our industry has seen from tax reform and regulatory relief," he said. "We should be creating more jobs, not wiping them out."

The Trump administration had said it intended its initial list of tariffs on $50 billion of Chinese products to have as little impact as possible on American consumers who purchase Chinese-made televisions, clothes and electronics. But ratcheting up the level of tariffs would eventually start to pinch consumers.

The tariffs could also damage investor confidence, potentially setting off **stock market** falls or persuading companies to withhold from investing in new facilities and factories. Already there are signs of strains in the global economy from the broader trade tensions, weakness that China and the United States are both better positioned to weather than other nations.

However, there's a chance Mr. Trump's tariffs may have a limited impact on China's nearly $13 trillion economy, which no longer depends as much on exports and can find other places besides the United States to sell its products.

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Shipping containers stacked in the Kwai Tsing Terminals in Hong Kong. | Jerome Favre/EPA-EFE, via REX and Shutterstock

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THE WALL STREET JOURNAL.

Markets

GE Drops Out of the Dow After More Than a Century; General Electric is being replaced by Walgreens Boots Alliance, in the latest setback for a troubled conglomerate that once had highest market value of any U.S. corporation

By Michael Wursthorn and Thomas Gryta
991 words
19 June 2018
06:34 PM
The Wall Street Journal Online
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English

General Electric Co. will drop out of the **Dow Jones Industrial Average** next week, a milestone in the decline of a firm that once ranked among the mightiest of blue-chips and was a pillar of the U.S. economy.

It will be replaced by drugstore retailer Walgreens Boots Alliance Inc., the latest sign of the rise of the global consumer economy and the postcrisis boom in debt issuance that has fueled a worldwide deal-making frenzy.

The decision to drop GE, an original member of the Dow that has been a part of the 30-**stock index** continuously since 1907, marks the latest setback for a company that once was the most valuable U.S. firm but has been hit hard in recent years by the unraveling of its finance business and competitive problems.

With the departure of GE and the addition of Walgreens, "the **DJIA** will be more representative of the consumer and health care sectors of the U.S. economy," said David Blitzer, chairman of the index committee at S&P Dow Jones Indices, the company behind the Dow. "Today's change to the **DJIA** will make the index a better measure of the economy and the **stock market**."

GE shares have tumbled 55% over the past 52 weeks, erasing more than $100 billion in wealth, as the company has switched leaders, slashed its dividend payment and pursued a restructuring that could result in a breakup of the struggling conglomerate. It is the cheapest stock of all 30 Dow components.

"We are focused on executing against the plan we've laid out to improve GE's performance," a GE spokeswoman said. "Today's announcement does nothing to change those commitments or our focus in creating a stronger, simpler GE."

Shares of GE fell 1.4% in after hours trading. While investors don't expect the company's departure from the Dow to be a long-term drag on its share price, some said its exit was a potent symbol of how far the company's elevated status in the U.S. economy has fallen.

"I think it tells you that GE no longer qualifies as one of the most important companies in our country," said Michael Farr, president of investment management firm Farr, Miller & Washington. "In a technology driven world, it has been challenging for manufacturing companies to remain relevant."

GE's market capitalization peaked at $594 billion in 2000, making it the most valued U.S. company. It has shrunk over the years. Under former CEO Jeff Immelt, the company shed its NBCUniversal media business and sold off most of its GE Capital arm, which was once one of the biggest U.S. lenders.

More recently, the Boston-based company struck a deal to sell its century-old railroad business, part of a plan to shed $20 billion worth of assets by the end of next year. It is also looking to sell its century-old lighting business.

Investors are waiting for a major portfolio update from CEO John Flannery, who took over last summer and continues to preach that "everything is on the table." Mr. Flannery has also been slashing jobs and cutting costs as GE struggles with slack sales in its big Power business, which sells turbines for power plants.

GE's decline has left it with a market value of $113 billion, but it wasn't the smallest industrial in the venerable index. GE's market cap and annual revenue are still larger than Dow member United Technologies Corp., which manufacturers Otis elevators and Pratt & Whitney jet engines.

GE's market capitalization is still nearly twice as large as Walgreens' valuation, though the two companies are about equal in terms of annual revenue. Walgreens, which dates back to 1901, has expanded in recent years by merging with European drug wholesaler Alliance Boots and buying up stores from rival Rite Aid Corp.

Walgreens ended Tuesday's session with a market value of $64 billion. It joins the index even though its larger drugstore rival CVS Health Corp. isn't a member. CVS is in the process of buying health insurer Aetna Inc. Walgreens has taken on debt as part of its growth through acquisition strategy: the company's long-term debt has increased to $12.5 billion as of February from $3.7 billion in August 2013, according to its SEC filings.

Component stocks of the Dow are selected by the index committee, a group that includes editors of The Wall Street Journal, which is published by Dow Jones & Co., a part of News Corp.

In 2015, the committee added Apple Inc. in place of AT&T Inc., which recently swallowed Time Warner Inc. The index has dropped several industrial members over the years, including Alcoa Inc. in 2013 and General Motors in 2009 after its bankruptcy filing.

The shake-up won't affect the value of the Dow, which fell 1.15% Tuesday and is down 0.1% this year. The index has surged to dozens of records in the past several years, most recently in January.

The change in the Dow's composition is unlikely to lead to an immediate shift in investor behavior. About $29.5 billion of mutual and exchange-traded funds track the Dow Industrials, a fraction of the $9.9 trillion in assets linked to the **S&P 500 index** through the end of 2017, according to data provided by S&P Dow Jones Indices.

Akane Otani contributed to this article.

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THE WALL STREET JOURNAL.

Markets

What Trade War? Skeptical Investors Convinced It's All a Negotiation; Unruffled by Trump's latest salvo against China, some investors stick to the view that threats are part of a process

By Akane Otani
521 words
19 June 2018
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The Wall Street Journal Online
WSJO
English

When the **stock market** tumbled on Tuesday after the Trump administration announced plans for additional tariffs on Chinese imports, many investors who thought a trade war would never happen started to lose their nerve and sold shares.

Then there are people like Craig Birk.

"We still believe the rhetoric and tactics are designed as part of a negotiation and that there is little appetite for an exchange of meaningful tariffs on either side," said Mr. Birk, executive vice president of portfolio management at Personal Capital.

James Bianco, head of Chicago-based advisory firm Bianco Research, agrees. Mr. Bianco last week described the conflict between the U.S. and China as "watching sausage being made"—a "nasty and ugly" process. Mr. Bianco said Tuesday, after the latest volley of threats between the U.S. and China, that appeared true "more so than ever."

For now, President Donald Trump is convinced he holds the upper hand and can eventually force China to concede and agree to better trade terms, Mr. Bianco said. "We've noticed that when Trump uses this blunt instrument, the power of the U.S., he gets what he wants," he said.

While Messrs. Birk and Bianco are holding firm, many of their peers said they are rethinking their previous skepticism that a trade war was at best a remote possibility after Mr. Trump called Monday for his administration to identify an additional $200 billion in Chinese exports to be targeted for tariffs.

"I think, for many of us, the assumption was perhaps that the tough talk was just going to be a negotiating position," said Ron Temple, head of U.S. equities and co-head of multiasset investing for Lazard Asset Management. "What's unnerving is that the trade dispute has broadened out well beyond China."

Jim Vogel, market strategist at FTN Financial, wrote to clients in April that "trade disruptions might impact the economy but not this year." Now, Mr. Vogel said, "the White House has done a 180 where the overall policy plan looks like it's about coming down hard, constantly and coming at everyone pretty much all at once."

Even the growing risk of a trade conflict can cause damage, potentially discouraging companies from proceeding with plans to expand their businesses.

Optimism about the outlook for global economic growth has waned recently after a string of soft data from the eurozone and China. The recent uptick in the dollar also raises the risk of sending further ripples through indebted emerging-market economies—something that could spark additional **volatility** in debt, equity and commodity markets in the coming weeks.

"The market earlier in the year thought this was just a negotiating tactic. Now it's becoming a bit more serious," said Liz Young, senior investment strategist at BNY Mellon Investment Management.

Ira Iosebashvili and Ben Eisen contributed to this article.

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THE WALL STREET JOURNAL.

Heard on the Street
Markets

For Stocks, It's the Economy Vs. a World of Hurt; Investors' high expectations for the U.S. economy have been met this year, but they were unprepared for the trouble on other fronts

By Justin Lahart
675 words
19 June 2018
11:17 AM
The Wall Street Journal Online
WSJO
English

Volatility has returned with a vengeance in the first half of 2018. Tuesday was no exception, with stocks down sharply on renewed worries about President Donald Trump's trade feud with China. Yet, for all of its whipping around, the **stock market** is even with where it was in early January. Considering how high investors had set their expectations, they should be pleased to have gotten off so easily.

The **stock market** has some things going for it right now, of course. Corporate tax cuts helped push profits up sharply—analysts polled by FactSet estimate second-quarter earnings for companies in the **S&P 500** will be up by 19% from a year earlier after rising 25% in the first quarter. Economic growth appears to have picked up too, with the effects of a strong job market and the personal income-tax cuts many Americans received combining to drive consumer spending.

But investors had already driven stocks sharply higher by the start of the year in anticipation of all this. What they hadn't anticipated were the other risks that would weigh on stocks. Chief among them are a Federal Reserve that is showing little timidity about raising rates, slowing growth overseas and the multiple trade skirmishes that Mr. Trump has embarked upon.

The Fed has raised rates by a quarter point twice already this year and policy makers are leaning toward raising them two more times. That is a conclusion that investors are coming around to: Futures markets now put the chances of two more hikes at 51%. Compare that with the start of the year when the odds of the Fed raising rates four times stood at just 10%.

And with inflation warming up and the unemployment rate on course to drop from an already extremely low 3.8%, the Fed will likely have to keep hiking when next year rolls around. That has helped push the yield on the **10**-**year** **Treasury** note to 2.88% from 2.41%. The 10-year yield might be higher still if it weren't for something else: Economic growth outside of the U.S. has begun to look a little less rosy.

Economists' growth forecasts for most major economies have fallen since the start of the year. That makes for slower global demand growth at U.S. multinationals' overseas operations. Compounding the problem, stronger relative growth in the U.S. has pushed the dollar higher, lowering the dollar value of the goods and services that U.S. companies sell abroad.

One particular area of concern on the economic front is China, which in the past has countered weakening global growth with stimulative policies. Now, though, it is tightening the screws on risky funding practices and damping its own growth as a result.

China is also the main focus of the administration's escalating trade disputes and so far its leaders are showing no sign of taking Mr. Trump's actions lying down. How that might affect the U.S. economy and U.S. companies is a wild card since there is no telling how far things will go before either country de-escalates or what pressure points that might emerge in global supply chains.

The trade troubles, along with the Fed's moves and weaker global outlook, have led investors to lower their expectations. The **S&P 500** now trades at 16.6 times expected earnings, according to FactSet, versus 18.2 times at the start of the year. That compares with a five-year average of 16.2, yet those were five years in which interest rates were significantly lower.

The **stock market**'s ability to absorb body blows therefore looks more limited at a time when it looks like the punches will keep on coming.

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THE WALL STREET JOURNAL.

Heard on the Street
Markets
The Other Yield Curve Investors Should Watch as Trouble Mounts; The Treasury yield curve is in focus. Here's the other curve investors should keep an eye on

By Richard Barley
367 words
19 June 2018
07:42 AM
The Wall Street Journal Online
WSJO
English

Escalating trade tensions have helped push the **U**.**S**. **Treasuryyield** curve to its flattest in more than a decade. This flattening is watched closely by investors as an indicator of economic trouble ahead. But another curve deserves attention too—and it is getting steeper.

That is the corporate-bond spread curve, which measures how much extra compensation investors are demanding to take credit risk at different time horizons. The U.S. curve has steepened, as spreads versus Treasurys have widened more on long-maturity bonds than they have on short-maturity bonds.

Investors now get 1.7 percentage points more yield than Treasurys for corporate debt maturing in 10 years or more, versus 0.68 point for one-to-three-year debt, according to ICE BofAML indexes. Three months ago, the gap was roughly one-fifth tighter.

The message this sends is that while investors have become more uncertain about the longer-term outlook, they are relaxed about the near term. The longer a corporate bond's maturity, the more credit risk it bears, since the underlying issuer's business or balance sheet can face more challenges over time. In good times, that risk seems distant; when investors start to focus on it again, it is a sign of a changing environment.

Some think ultraloose global monetary policy has distorted the Treasury curve, potentially generating a false signal. So another indicator for investors to watch is valuable. For now, the credit curve only seems likely to get steeper, in particular because companies have issued a lot of risky long-dated debt. The size of the U.S. triple-B-rated 10-year-plus index has surged to $878 billion, from $235 billion 10 years ago.

The danger point is a combination of wider credit spreads and a flatter credit curve, which would signal deeper concerns about company balance sheets. The good news is this isn't something corporate-bond investors are betting on—yet.

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THE WALL STREET JOURNAL.

Business

Sarepta Gets Boost From Early Trial Results on Muscular Dystrophy Treatment; Biopharmaceutical firm's stock jumps nearly 40% on positive early stage trial

By Aisha Al-Muslim
544 words
19 June 2018
05:59 PM
The Wall Street Journal Online
WSJO
English

Sarepta Therapeutics Inc. gained about $2.5 billion of **stock market** value Tuesday after an early stage trial of a gene therapy showed promise in its ability to treat patients with Duchenne muscular dystrophy.

Sarepta said study results showed the therapy helped patients with the crippling disease significantly reduce levels of creatine kinase, an enzyme associated with muscle damage caused by the disorder. Results also showed patients receiving the treatment had robust levels of a protein key to muscle function. No serious adverse events were observed in the study, the Cambridge, Mass., biopharmaceutical company said.

The results are from a trial that featured only three children. To get regulatory approval for the treatment, Sarepta may have to conduct additional tests with larger patient pools.

"Although the data are early and preliminary, these results, if they persist and are confirmed in additional patients, will represent an unprecedented advancement in the treatment of DMD," said Jerry Mendell, a neurologist at the Nationwide Children's Hospital in Columbus, Ohio, in prepared remarks. Dr. Mendell was among several speakers at the company's event highlighting Tuesday its research and development efforts.

Sarepta shares surged 36% to close at $143.93 on Tuesday. The gains value the company at about $9.4 billion. Shares of Sarepta have more than quadrupled in the past year.

Sarepta's news also helped drive the share price of Solid Biosciences Inc. up 46% in Tuesday trading, bringing that company's market capitalization to about $1.5 billion. The stock also closed higher Monday after the Food and Drug Administration lifted a clinical hold on its Duchenne muscular dystrophy treatment after it addressed agency questions regarding study results after an adverse event was reported with a patient.

Sarepta's results highlight the "strong promise" of the company's gene therapy and should position the company as a leader in the field, according to a note from Boston-based health-care investment bank Leerink Partners.

Duchenne muscular dystrophy is a rare, fatal genetic disease that causes progressive muscular weakness, typically in male children. It is estimated that it affects about one in 3,600 boys world-wide. By adolescence the disease leaves many of its victims in wheelchairs and frequently kills patients by the time they are in their 20s or 30s.

Pat Furlong, founding president and chief executive of Parent Project Muscular Dystrophy, called the early results "encouraging" in prepared remarks. Parent Project Muscular Dystrophy committed $2.2 million to the clinical trial with support from additional Duchenne foundations and families.

Sarepta, which focuses on development of precision genetic medicine to treat rare neuromuscular diseases, has a history with treating Duchenne muscular dystrophy.

In September 2016, the U.S. Food and Drug Administration gave accelerated approval to Sarepta for the first Duchenne muscular dystrophy drug after overcoming concerns about its small study size.

The company had leveraged the emotional appeal of the parents' stories to push for approval for the drug, which is called eteplirsen, a $300,000-a-year treatment for the disease.

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THE WALL STREET JOURNAL.

Markets

Icahn Wins Majority on SandRidge Board; Activist investor gets four seats in a shareholder vote and is awarded a fifth by the company

By Cara Lombardo
631 words
19 June 2018
07:17 PM
The Wall Street Journal Online
WSJO
English

Carl Icahn won a majority of seats on SandRidge Energy Inc.'s board, the company said Tuesday.

The activist investor won four board seats in a shareholder vote and the oil-and-gas company agreed to give him a fifth after another was too close to call. SandRidge held on to three seats after striking a deal with Mr. Icahn to expand the board by one.

The Wall Street Journal reported earlier Tuesday that Mr. Icahn was expected to win at least four of seven seats.

Mr. Icahn, who has criticized the Oklahoma City company's deal making and executive pay, had aimed to replace the entire board with his own nominees.

He is SandRidge's largest investor with a roughly 13.5% stake.

It is rare for activist investors to succeed at replacing an entire board, but it has happened, including at Darden Restaurants Inc. in 2014 and at retailer Destination Maternity Corp. earlier this year. It is even unusual for activists to win control of a board as Mr. Icahn apparently has at SandRidge. The billionaire activist has done so through a proxy fight only four times in his career, according to activist research firm 13D Monitor.

SandRidge had early success in the American shale boom but a protracted **oil-price** slump led it to bankruptcy in 2016. It emerged later that year and now has a market value of about $590 million. SandRidge shares, which were down about 25% this year through Monday, rose 7.5% to $17.02 on Tuesday.

Mr. Icahn had been vocal in his opposition to SandRidge's since-abandoned bid to buy Bonanza Creek Energy Inc. last year and its rejection of an unsolicited offer from Midstates Petroleum Co. in March. The company has since said it is open to a full or partial sale of itself.

While Mr. Icahn initially called on two of SandRidge's then five board members to resign, his plans escalated and by April he aimed to replace the entire board. SandRidge agreed to expand the board to seven seats and run two of Mr. Icahn's independent nominees on its own slate, effectively agreeing to give him those seats.

The new Icahn board members are Randolph Read, John Lipinski, Jonathan Christodoro and Bob Alexander and Jonathan Frates. Existing SandRidge board members Sylvia K. Barnes, David Kornder and William M. Griffin, who has acted as chief executive officer since the former CEO left in February, retained their seats.

The two primary shareholder advisory firms, Glass Lewis & Co. and Institutional Shareholder Services Inc., recommended shareholders back some of each side's nominees.

The SandRidge contest was closely watched not only because Mr. Icahn sought to replace an entire board but also because it was one of the highest-profile proxy fights so far to use so-called universal ballots, which allow investors to select a mix of nominees backed by either side. Though companies and activists alike have said universal ballots could improve shareholder democracy, the SandRidge vote underscored that they could bring their own set of complications.

SandRidge on Monday accused Mr. Icahn of urging shareholders in private meetings to reallocate their votes from candidates supported by the proxy advisers to those who weren't, a move the company said was meant to take advantage of all the names being on the same card to give him control of the board. Mr. Icahn in response issued a statement saying SandRidge seemed to be complaining that shareholders could use the universal ballot as intended—to vote for their own combination of nominees.

Write to Cara Lombardo at cara.lombardo@wsj.com

Document WSJO000020180619ee6j00439

THE WALL STREET JOURNAL.

World

Trade Fight With U.S. Complicates China's Campaign to Contain Debt; Recent economic expansion seems to be ebbing, triggering calls for Beijing to reopen credit spigot before trade conflict further dents growth

By Lingling Wei
1,210 words
19 June 2018
10:57 AM
The Wall Street Journal Online
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English

BEIJING—A bruising trade fight with the U.S. lands at a difficult time for China as its economy contends with rising headwinds, constraining Chinese President Xi Jinping's options.

While Chinese officials have been bracing for a trade war for months—promising to match the Trump administration measure for measure—signs are rising that China's recent economic expansion is ebbing, from weakening investment and household consumption to increasing corporate defaults, in part due to a key Xi initiative to contain debt and fend off financial risks.

That slowdown is triggering mounting calls from some corners of the government for Beijing to reopen the credit spigot and ease off on Mr. Xi's program before the trade conflict further dents growth.

"It's a testing moment for Beijing," said Larry Hu, China economist at Macquarie Group, a Sydney-based investment bank.

Soaring levels of corporate and local government debt are seen by economists as potentially dragging down the world's second largest economy. Getting a handle on debt has been a Xi priority.

The Trump administration's simultaneous fights with the European Union, Canada, Mexico, Japan and others on trade give Beijing some breathing room, making it less likely that those traditional U.S. allies will mount a broad front against Chinese trade practices widely seen as unfair. It also gives the Chinese leadership a chance to pick up potential partners against Washington.

The domestic back-and-forth over whether to press ahead or ease off on the campaign to reduce debt underscores the balancing act facing the Chinese leadership as it tries to fight a trade war with the U.S. while keeping China's economy from tanking. President Donald Trump has said that the U.S., with its economy steaming ahead, is in a strong position in a trade contest.

The latest volleys from Mr. Trump, who said Monday that he had directed aides to identify $200 billion in Chinese goods for new 10% tariffs, caught Beijing off guard. Officials scrambled to put together a strongly-worded response, pledging to fight back forcefully without giving any details.

By escalating the tariff threats to potentially $200 billion in Chinese goods, the Trump administration is in effect driving Beijing to look for penalties other than tariffs; the U.S. exports about $150 billion in goods to China.

Beijing could restrict access to China's market by American companies, tie up firms already in the China market in antitrust and other regulatory red tape and try to steer business to other foreign firms. The Trump administration already accuses Beijing of unfair practices so targeting American business would reinforce that perception, likely hardening the response.

Early Tuesday, hours after the Trump announcement on additional tariffs, the People's Bank of China pumped 200 billion yuan, or $31 billion, of one-year funds into the nation's banks.

Advisers to the central bank said the move didn't mean the bank was loosening its conservative monetary stance, but was aimed at calming jittery investors and containing any financial fallout from the trade fight.

Still, the unusually-large liquidity injection surprised market participants, helping drive down the yuan's value against the dollar to its weakest level in five months, at 6.4743 per dollar. The benchmark Shanghai Composite **stock index** plunged 3.8% Tuesday, dipping below 3,000, a psychologically-important level for investors and hitting its lowest mark in two years.

Meanwhile, news items containing "China-U.S. trade war" were temporarily deleted from searches on the popular Baidu Inc. search engine. The searches were restored late Tuesday. Baidu declined to comment.

To fend off an economic slowdown, some officials in the State Council, China's cabinet, are urging more aggressive loosening measures to boost lending and spur growth, such as reducing the portion of deposits banks are required to hold in reserve. Others, notably those at the central bank and other financial regulators, want to stay the course of debt control.

Yi Gang, China's newly appointed central-bank governor, told a closed-door meeting of prominent U.S. and Chinese economists in March that his "first task" was to keep a lid on credit growth, according to people present.

That effort has slashed borrowing between banks, crimping practices that enabled smaller lenders to ramp up risky borrowing and lending. The pain that has caused has started to show up in recent months, with more businesses having trouble getting financing.

Companies ranging from property developers, local-government financing vehicles to manufacturers recently have missed payments on either bank loans or bonds, even though overall default rates remain low.

"Financial deleveraging is now trickling down to the real economy," said Sheng Songcheng, a senior adviser at China's central bank. "All those efforts would go to waste if monetary policy gets loosened now."

In looking for options to deal with the Trump administration, Beijing has studied the U.S. trade fight against Japan in the 1980s and 1990s, according to Chinese officials. Back then, Tokyo accommodated Washington's demands by appreciating the yen and then subsequently unleashed fiscal stimulus to help the economy withstand the pressure from a stronger currency. Those actions led to a housing bubble that helped sink the Japanese economy.

"Every country now realizes when the U.S. launches punitive tariffs, you must retaliate," said Yukon Huang, senior fellow at the Carnegie Endowment in Washington. "You both lose. If you don't do that, only you lose."

How China adjusts its economic policy, officials and economists said, will depend on how much worse the trade fight with the U.S. becomes. Strong exports buoyed the Chinese economy last year, keeping expansion at 6.9% above the leadership's growth target of 6.5%.

Recent snapshots of economic activity show that investments in Chinese factories and other fixed assets have slowed to the lowest level in 18 years and China's household consumption, which has been steady in recent years, is starting to decelerate sharply.

With exports likely to take a hit too, policy makers have put in place tax cuts and other measures aimed at boosting consumption. If the conflict escalates to include $200 billion of Chinese exports, Deutsche Bank AG estimates that would shave between 0.2 and 0.3 percentage point from China's annual GDP growth.

"If the trade war gets worse from here, China's policy makers will be forced into easing," said Zhang Zhiwei, Deutsche Bank's chief China economist. "That will probably delay the current policy agenda of deleveraging and containing financial risks."

Chao Deng contributed to this article.

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THE WALL STREET JOURNAL.

Economy

U.S. Housing Starts Rebound in May; Residential building permits—potentially signaling amount of construction is in the pipeline—fell 4.6%

By Sharon Nunn
599 words
19 June 2018
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The Wall Street Journal Online
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U.S. housing starts rebounded last month to the highest level since 2007, driven by a construction rebound in parts of the country that have lagged for much of the economic recovery as well as a lingering apartment boom.

Housing starts rose 5% in May from the prior month to a seasonally adjusted annual rate of 1.35 million, the Commerce Department said Tuesday. Compared with a year earlier, starts were up 20.3%.

The strong improvement was spread fairly evenly between single-family and multifamily, despite expectations that builders would pull back on new apartment construction given a flood of new units already hitting the market. Single-family construction increased 3.9% in May compared with a month earlier, while multifamily building increased 11.3%, according to the Commerce Department.

Midwestern builders also significantly ramped up construction, good news for a region that had lagged compared with the South and the West through much of the economic recovery. Housing starts in the Midwest increased 62.2% in May compared with a month earlier—albeit with a 28.1 percentage point margin of error.

Wells Fargo & Co. Senior Economist Mark Vitner said part of the bump in the Midwest may be attributable to an improving manufacturing sector. "The economic recovery has broadened and it's reached parts of the country that hadn't seen improvement until recently," he said.

Housing-starts data are **volatile** from month to month and can be subject to large revisions. May's 5% jump for starts came with a margin of error of 10.2 percentage points.

Building permits, which tend to be a more reliable indicator and signal how much construction is in the pipeline, declined 4.6% to an annual pace of 1.301 million last month. Permit declines in the South and West drove May's permits figure lower. Permits last month fell for both single-family and multifamily housing.

Nonetheless, housing construction appears on track to have a slightly better year than many economists had predicted, thanks in part to surprisingly strong multifamily growth.

Overall starts grew by 11% in the first five months of 2018 compared with the same period a year earlier. Multifamily starts rose 13.3% during that period, while single-family starts rose 9.8%.

Still, builders face headwinds in the coming months. Rising lumber prices have added nearly $9,000 to the cost of a new home since January 2017, according to the National Association of Home Builders, which reported on Monday that builder confidence ticked down slightly in June.

Mr. Vitner said larger home builders have more power to negotiate deals on material and labor prices, but smaller builders are struggling.

"A lot of smaller builders are having to postpone projects…and say let's just sit this out and see if prices come down," he said.

Higher mortgage rates make it more expensive for home buyers, potentially damping demand if the trend continues. "Rising costs for land, labor, and materials are making it difficult to build entry-level and affordable homes…This is on top of prices that are rising due to strong demand and limited availability of homes," said Danielle Hale, chief economist for Realtor.com.

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Sharon Nunn contributed to this article.

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The New York Times

Business/Financial Desk; SECTB
Small Companies' Shares Are Strong on a Mixed Day

By THE ASSOCIATED PRESS
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19 June 2018
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NYTF
Late Edition - Final
5
English

Stocks in the United States shrugged off early losses and wound up with a mixed finish on Monday. Household goods companies took some of the worst losses as the **Standard & Poor's 500-stockindex** fell for the third time in four days.

The **S.&P. 500** dropped as much as 22 points early on. Consumer products and packaged-foods companies stumbled and drug makers and distributors fell, as did health insurers. That came after indexes in Europe and Asia fell. German stocks took steep losses as investors wondered if a dispute over migrants could eventually threaten the German government.

But stocks gradually recovered most of their losses as energy companies rose along with **oil prices** and technology companies managed to make some gains as well. Smaller and more United States-focused companies climbed higher. That continued a pattern that has persisted for more than three months.

It's been a turbulent few months for stocks, but the benchmark **S.&P. 500** is a bit higher than it was when international trade tensions started to weigh on the market in late February. Terry Sandven, chief equity strategist at U.S. Bank Wealth Management, said it's a good sign that some sectors that have struggled are now doing better.

''It's indicative of a market that's unconvinced that a trade war will develop,'' he said. Still, he said the next month of trading could be choppy as investors analyze the latest trade developments and wait for companies to start reporting their second-quarter results in mid-July.

The **S.&P. 500** fell 5.91 points, or 0.2 percent, to 2,773.75. The **Dow Jonesindustrial average** dropped 103.01 points, or 0.4 percent, to 24,987.47. The **Nasdaq composite** edged up 0.65 points to 7,747.03.

The Russell 2000 index rose 8.55 points, or 0.5 percent, to a record 1,692.46. Many investors feel the smaller and more United States-focused companies in that index would be less vulnerable if a major trade dispute were to slow growth in the global economy. Most of the companies listed on the New York Stock Exchange closed higher.

The drug maker Biogen suffered the biggest fall of any **S.&P. 500** company after positive clinical trial results from a competitor, PTC Therapeutics. Its stock jumped 27.5 percent to $47.88 after it reported on an early study of a drug intended to treat Type 1 spinal muscular atrophy, a genetic disorder that affects infants. PTC's drug could affect sales of Biogen's Spinraza, and Biogen lost 5.2 percent to $289.12. Its partner Ionis Pharmaceuticals sank 6.4 percent to $43.61

Oil futures rose as investors waited for an OPEC meeting later this week. Benchmark United States crude added 1.2 percent to $65.85 a barrel in New York. Brent crude, used to price international oils, climbed 2.6 percent to $75.34 a barrel in London. Gold rose 0.1 percent to $1,276.20 an ounce.

Bond prices were little changed. The yield on the **10-year Treasury** note stayed at 2.92 percent.

The dollar fell to 110.55 yen from 110.62 yen late Friday. The euro inched up to $1.1616.

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)

Document NYTF000020180620ee6j0000j

THE WALL STREET JOURNAL.

Economy

Tariffs Start to Ripple Their Way Through the U.S. Economy; Effects are like a tax increase, very small at this point, but reducing real GDP and eroding real wages

By Josh Zumbrun
1,333 words
19 June 2018
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English

In recent weeks, several major rounds of tariffs have moved from proposals to realities, and major new tariffs have been threatened—shifting the stakes for President Donald Trump's trade actions on the U.S. economy.

Tariffs raise the price of imported goods, increasing costs to consumers, and making domestic producers (who don't face the tariff) more competitive.

Examples of how new tariffs might ripple through the economy have already been provided by earlier, smaller rounds of tariffs. These earlier examples also show why broad effects from tariffs, on the otherwise booming U.S. economy, might be hard to detect.

One of the first to go into effect under Mr. Trump came in January, with the imposition of 20% tariffs on washing machines.

While tariffs are formally paid by whomever imports the goods, the importers can pass their costs along to consumers. In the case of washing machines, that happened quickly: The index for laundry equipment in the Labor Department's consumer-price Index, the nation's main gauge of inflation, shot up by about 17% over the past three months.

That is by far the biggest three-month gain in laundry equipment in data going back 12 years. But it comes at the end of a period in which prices had mostly declined for years. Those price declines, driven by foreign-made products, had placed domestic appliance producers under pressure to begin with.

The surge, though sharp and clearly inflationary, only put washing machine prices back to where they had been in June of 2015.

As with any major appliance, consumers don't buy them very often, and likely don't notice month-to-month price swings. Major appliances are just one-tenth of 1% of the consumer-price index.

"Certainly in some industries, or good by good, it has some material effect," said Stephen Gallagher, managing director of Société Générale. "In my view it's still not a macro event, though it could develop to that…right now it's still more of a temper tantrum on trade, as opposed to a real war."

Mr. Trump's steel and aluminum tariffs were announced March 1. For some countries they went into effect quickly. The European Union, Canada and Mexico were given more time to negotiate, but those extensions expired at the beginning of this month.

Prices for different types of steel and aluminum began to climb almost immediately, posting the biggest three-month price increase that has been recorded in years. While clearly inflationary and unwelcome for metal consumers, the jump in prices isn't that much larger than typical **volatility** in the metals. And only a small portion of the metals ends up in consumer goods.

Even though a car contains several hundred pounds of aluminum, for example, auto prices haven't notably increased since the tariffs began. Car sales are down slightly, but that probably owes more to higher interest rates than to any consumer awareness of the impact of aluminum tariffs.

In public appearances, Commerce Secretary Wilbur Ross has carried around cans of Campbell Soup, holding them up and saying they have only a few pennies worth of steel in them. The effects are negative for the soup company—Campbell's stock has fallen 14% since February, and the company has cited steel tariffs specifically as something that will be a hit to its bottom line—but Mr. Ross's broader point is that most consumers won't notice.

The hit to companies like Campbell's is why the effects of the tariffs tend, overall, to reduce jobs. Far more U.S. companies consume steel than produce it. By increasing their costs and reducing their profits, the tariffs have the knock-on effect of making firms less likely to hire, economist say.

As of mid-2017, there were 29,288 steel-consuming firms, employing over 900,000 workers who face higher prices versus just 916 steel-producing firms with 80,000 employees who benefit from those higher prices and reduced competition.

Despite being a direct beneficiary of the washing-machine tariffs, Whirlpool Corp. is also a metal consumer. Its **stock price** jumped about 12% when the washing-machine tariffs were announced but is down 18% since. In its first-quarter earnings call in April, Whirlpool said the steel and aluminum tariffs would cost the company an extra $50 million.

The effects are also like an inflationary tax increase, very small at this point, but reducing real gross domestic product and eroding real wages.

Those steel and aluminum tariffs are widening now that Canada, Mexico and the European Union are hit. As of last week, tariffs have also been applied to about $50 billion of Chinese imports. Add this all up, and it's likely to be a noticeable uptick in the effective tariff rate.

Mr. Gallagher of Société Générale has estimated that the new rounds of tariffs will push the effective U.S. tariff rate, as measured by tariff revenue as a percentage of all imports, to 2% from about 1.5%.

It would be the biggest and sharpest increase in taxes on customs in well over 30 years, but it would only take trade restrictions back to where they were in the late 1990s.

Mr. Gallagher's calculations do not include the latest proposal for tariffs on as much as $400 billion in Chinese imports, nor proposed tariffs on autos. For now, those tariffs remain just threats.

The effects remain muted because tariffs, so far, still affect only a small portion of the roughly $3 trillion a year in imports that the U.S. is on course to bring in this year. U.S. imports are about 15% of gross domestic product, compared with a world average of 28%, according to World Bank data. In other words, despite running by far the world's largest trade deficit, the U.S. economy is less reliant on trade than most nations.

In a new analysis, Mark Zandi, chief economist of Moody's Analytics, modeled the effects of different trade policy scenarios on the overall U.S. economy.

His findings show that, in the context of a roaring economy, the negative impacts will be hard to notice.

The tariffs announced so far would cost the economy about 145,000 jobs by the end of 2019, Mr. Zandi's analysis concluded. That is less than the total number of jobs created in the broader economy in an average month.

If tariffs expand to $100 billion extra of Chinese imports, as well as to other threatened goods such as autos, then the effect grows, costing the economy over a half million jobs by the end of 2019. Mr. Zandi's analysis was completed before Mr. Trump announced the possibility of tariffs on $400 billion more of Chinese goods.

But the labor market is booming, and even under the scenario with $100 billion in extra imports targeted for tariffs, the economy is still forecast to add about 2.5 million jobs over the next 18 months. It's just that without tariffs, it would add 3 million, in Mr. Zandi's analysis.

The basic effects of the tariff "are just like a tax increase," said Mr. Zandi, "But we had a very massive tax cut, deficit-financed, that's temporarily juicing things up this year and next year, and you're just taking some of that away."

In the scenario of expanding tariffs, GDP would be about 0.34% lower, by the end of 2019.

"It's all negative," Mr. Zandi said, "but right now, the dollars and cents are small in the grand scheme of things."

Write to Josh Zumbrun at Josh.Zumbrun@wsj.com

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THE WALL STREET JOURNAL.

U.S. Markets
Markets
Escalating Trade Threats Slam Global Shares; Dow industrials drop sharply following selloff in Asian markets

By David Hodari and Allison Prang
678 words
19 June 2018
05:22 PM
The Wall Street Journal Online
WSJO
English

* Fresh tariff threats batter global stocks

* Industrials, materials sectors worst in S&P

* Safety sectors close higher

Global stocks dropped Tuesday as trade tensions between the U.S. and China intensified, sparking selling from Shanghai to New York.

The declines came after President Donald Trump raised the stakes in Washington's trade conflict with China, asking his administration on Monday to draw up a fresh list of Chinese goods worth $200 billion on which to impose tariffs.

That move marked the latest in a series of back-and-forth measures between the countries that left investors around the globe worried the conflict would escalate into an all-out trade war.

The **Dow Jones Industrial Average** tumbled 287.26 points, or 1.1%, to 24700.21, notching its longest streak of consecutive declines since March 2017. The **S&P 500** fell 11.16 points, or 0.4%, to 2762.59 and the **Nasdaq Composite** lost 21.44 points, or 0.3%, to 7725.59.

Shares of industrial and materials companies in the **S&P 500**, which analysts fear could take a heavy hit under a trade war, fell 2.1% and 1.8% respectively. Utilities, real estate and consumer staples—groups that investors often buy in times of market **volatility**—all climbed, along with shares of telecom and health-care firms.

Kate Warne, investment strategist for Edward Jones, cautioned investors against changing their holdings substantially, given that the tariff threats might not actually take place.

"It's hard to tell whether these announcements are all negotiating positions and we'll see some set of discussions to basically lower the temperature," Ms. Warne said.

The declines in the U.S. stocks came after Asian investors dumped Chinese stocks, sending the Shanghai Composite Index down to its lowest level in almost two years, while the Shenzhen A Share index shed 5.8%. Investors also unloaded stocks elsewhere, with the Stoxx Europe 600 closing down 0.7%.

Trade concerns were among the risks highlighted by European Central Bank President Mario Draghi on Tuesday, when he said the bank could extend its bond-buying program again and delay any interest-rate increases amid mounting economic risks. The comments, days after the ECB laid out plans to phase out its bond purchases, underline the bank's caution in winding down a major stimulus program just as the region's economy appears to be slowing.

While the impact of the trade dispute for U.S. consumers has so far been muted, firms across the world would feel the effects if Washington and Beijing implement their proposed levies, according to Paul Donovan, chief economist at UBS Global Wealth Management.

"Non-Chinese companies, including U.S. companies, are just as likely to be affected by taxes on Chinese goods, given the complexity of modern supply chains," Mr. Donovan said in a note.

Government bonds strengthened, with the yield on the benchmark 10-year U.S. Treasury note falling to 2.893%, compared with 2.926% Monday. Yields fall as **bond prices** rise.

With strong growth and an interest-rate increase last week from the Federal Reserve, the WSJ Dollar Index, which measures the U.S. currency against a basket of 16 others, was last up 0.2%, extending its five-day climb to 1.1% .

If U.S. tariffs do begin to squeeze the Chinese economy, "the fear would be that China could be tempted to devalue its currency as a support mechanism for its economy," said Lee Hardman, currency analyst at MUFG.

Hong Kong-listed ZTE Group plummeted 25% after the U.S. Senatevoted to reinstate a ban on selling U.S. parts to the Chinese telecom company. The move marked the rejection of a deal between Mr. Trump and Beijing to save the firm.

Saumya Vaishampayan and William Mauldin contributed to this article

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Economy

Transcript: Media Q&A With Atlanta Fed's Raphael Bostic in Savannah; Official discusses his outlook for interest rates and the flattening of the yield curve

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Federal Reserve Bank of Atlanta President Raphael Bostic answered reporters' questions after speaking at a Rotary Club of Savannah event in Georgia on Monday, June 18, 2018. He talked about his outlook for interest rates, the flattening of the yield curve in the bond market and Federal Reserve Chairman Jerome Powell's decision to hold a press conference after every policy meeting. Here is a transcript of the exchange, lightly edited for length and clarity.

Q: (In progress) – and there's – people submitted forecasts on three or four increases. You have been at three increases. Is that where you still are?

RAPHAEL BOSTIC: I'm still at three, yes. You know, as I've said, you know, we're going at a nice steady pace, and I'm going to let data inform how practically I think we need to be moving toward neutral. I started at two at the beginning of the year, and with the stimulus I moved to three, and I haven't seen anything to suggest that I think we should do more than that at this point.

Q: So if I could ask about sort of neutral. And I think you pinned your estimate around 2½ percent, right?

MR. BOSTIC: So somewhere in that range.

Q: Somewhere in that range.

MR. BOSTIC: So, you know, the estimates we have are anywhere between 2¼ to three. So 2½, 2¾, somewhere in that space.

Q: So my question is, as you rise up to it, how are you going to – I'm thinking here that the sessions kind of get backdated, right? The NBER [National Bureau of Economic Research] calls a recession when you're in it. So how are you going to satisfy yourself that you can call neutral before you get into it or before you step over the line? And is that what you're aiming to do? Because it seems like everyone wants to kind of glide in there and stop right at or before.

MR. BOSTIC: So this is a – this is a debate I'm having with my staff, exactly this question. I think my view is I want to make sure that we do all that we can to not miss something that suggests that the economy is in a position where a more aggressive or too aggressive stance puts the brakes on growth and causes the recovery to not be sustained.

So we're actually doing a lot of work right now to see, well, what kind of metrics are there to give us signals about weakness in the marketplace and where the market thinks – and those moments when the market thinks there are weaknesses. So things like futures, markets on fed-funds path and the like. Those are things that give us additional clues beyond the obvious direct real statistics that you get on GDP [gross domestic product] and wage growth and employment.

So, you know, as I said today, I think our job has gotten a lot harder. All the easy stuff has been done. And so now we have to, I think, be more diligent and more creative around what kind of inputs we're going to embrace to understand how the economy is performing.

Q: So just to clarify, you said 2¼ to 3 percent is the range that you look at as neutral?

MR. BOSTIC: That's what our models are saying, yeah.

Q: Is that the SEP [Fed's summary of economic projection] models or the Atlanta Fed's models?

MR. BOSTIC: The Atlanta Fed's models.

Q: OK, 2¼ to 3.

MR. BOSTIC: Mmm hmm.

Q: That's a pretty wide range and it pretty much encompasses the – like the range, I think, from the SEP, right, which is like 2.3 to 2.9?

MR. BOSTIC: Something like that, yeah. Yeah, so the SEP is – you know, that's an aggregation. And, you know, what we try to do with those long-run – I'll tell you what we try to do, is we look and we try to carve out a pathway, but then also use our models and try to just benchmark sort of what looks like something that is not going to be too extreme. But I would say, you know, all of these things, there is – how do I want to say this? I think – I think there's a fallacy of too much precision. And so we're really trying to understand sort of the general area, and then we let the information that comes in as the – as the economy performs give us insights as to whether there's still space to move or whether we should be more cautious.

Q: I guess this kind of changes gears a little bit, but I know we've talked about the yield curve, and it just keeps coming up, and it just keeps flattening. Do you think that it's – like, what importance do you think the slope of the yield curve is playing on the Fed's assessment of the prospective rate –

MR. BOSTIC: So I can't talk about the whole Fed. I can tell you sort of how I –

Q: Yeah, yeah. Of course. (Laughs.)

MR. BOSTIC: And I – and I would say there are few things I get asked about more than the yield curve, all right –

Q: Yeah. (Laughs.)

MR. BOSTIC: – and the flattening of the yield curve. And so I asked our staff – you know, I went back after one of these things and I said, you know, I'm getting a lot of questions on this – (laughter) – and we need to have a view as to sort of where this is. And we're still working through that. I think we're going to come out with a blog series on this in a couple of days and just try to explain some of our thinking about it.

But I would say a couple things. First, the yield curve, these prices are a signal of other things, all right? In and of themselves, I think you need to – you want to try to get underneath to understand what they're signaling and what applications that has for the broader – for broader economic performance.

A second thing is that, you know, some of the – some of the factors that generate the yield curve in terms of perceptions of risk premia, the term premium and the like, those have evolutions that are on some level – can be driven by things that are independent of Fed policy and often independent of sort of economic performance. So, you know, geopolitical risk can inform those things. And we're also trying to disentangle all of those additional things to see if there is some core element of the yield slope that is more informative.

But we're actually – we're still working through this. And this is one of the things – you know, I mentioned today the natural rate of unemployment is something that's uncertain and you have – we try to look at that indirectly. Detailing what parts of the yield curve are most important, that's something else.

But a third thing I did want to say is I know that most of the markets look at this, right? And so this is not something that I think we can afford to be too cavalier with in terms of thinking that this time is obviously different, right? Because to the extent that the – look, there may be people who believe that. But if a broad part of the market doesn't, then by not taking that sufficiently seriously it could trigger its own response, which would potentially increase **volatility** in the marketplace.

Q: So I was – going back to the sort of – the sort of neutral-rate discussion for a second, a kind of related theme. What are you insuring against right now? I mean, if you're – if you start edging up close to neutral, right, and the sort of default setting for the last few years has been whatever we do we don't want to crimp the recovery, is it fair – is it a fairly strong consensus that you want to stop before? Does the Fed feel it wants to stop before it gets to neutral to ensure you don't put any – don't have any risk of going over the line?

MR. BOSTIC: So I don't – I don't want to necessarily stop before neutral. I think, for me, you know, I wasn't here for much of the run-up in the fed-funds rate, but at that time I think the view was the economy was relatively weak and it needed to have a considerable amount of stimulus. As time has passed, the economy has obviously strengthened, and so the amount of stimulus that's required is far less than it was before. And, you know, given our performance metrics, I don't think it's a stretch to argue that it doesn't need any stimulus, right? So stopping before we get to that level, given how the economy's performing, I think would not be consistent because a stimulus would suggest we want it to go further than what it is. And I think at this point I'm comfortable to let the economy work how it's going to work and be open to a response in either direction.

Q: So a neutral setting and let's see what happens?

MR. BOSTIC: Exactly. And if there's a sign that there's some overheating, then we continue to go. And if there's signs of weakness due to uncertainty or other things, then we can pull back.

Q: And if I could just push you on this, the second. In his – I forget if it was a confirmation hearing or one of the appearances before Congress – [Fed] Chair [Jerome] Powell said we're really trying to explore the frontier here of unemployment, right? And there's this broad uncertainty around the neighborhood, how low it could go. You put this very eloquently, saying, I think last time we talked, six million people unemployed; that's a lot of people unemployed. Are you insuring against the wrong thing by going to neutral at this point? Should we be insuring against allowing those people to get back to work, insuring in favor on that?

MR. BOSTIC: So I think – so, no, I don't think that's right. And largely because what we know is that if the economy gets to an overheated stage, all those extra people who are trying to get employed will lose their jobs, plus a whole lot of other people. So the snapback impact or effect can be significant and fully counterproductive. So we need – so, from my view, if we can improve the labor-market outcomes while avoiding the overheating situation, that's fine. But again, I think that we all should have caution with the idea that, you know the Fed has that amount of nuanced ability to change and affect market trajectories.

So that's why I think we're – the cautious here, the slower is the right way to go because the economy gives momentum. And to the extent that we facilitate extra momentum, that makes it harder for us to pull back and get – and avoid the dislocation of the pain that has historically happened when that overheating turns into the snapback.

Q: So you would favor pausing, though, when you get to what appears to be neutral?

MR. BOSTIC: Yeah. I've said this before. You know, I'm going to let the data inform the extent to which the economy needs extra stimulus or it needs some more restrictive policy stance on our position.

Q: Since the beginning of the year, the data have really kind of moved in a noticeably firmer kind of direction in terms of showing, you know, consumer spending picking up. Inflation has hit 2 percent for two straight months. The CPI [consumer-price index] is closer to 3. You know, as you mentioned in your speech, personal consumption spending, business spending, those have all picked up. The one thing that has – a lot of people say has changed the least are the Fed's kind of policy statements. I don't know if you can answer this, but, you know, has there been any kind of change in the tone of the meetings that maybe isn't kind of reflected in the policy statement? You know, have the discussions become more heated or more animated?

MR. BOSTIC: Yes, I'm not – I'm not going to speak to that. What I would say is, you know, this last statement had a pretty significant change relative to where we were before, and it took out a lot of the language that was the forward guidance type language that was present when we were close to zero. I think that's a signal of – you know, of our recognition that all the things you said are right. The economy is firmer, is performing better. And, as a consequence, we have to talk about our policy position and stance in a different way.

Q: So it was also announced by Chairman Powell that you're going to do press conferences at every meeting. What do you make of that?

MR. BOSTIC: I think it's a good thing. You know, I know that the market has come to a view that the FOMC [Fed's rate-setting Federal Open Market Committee] will not move unless it's a press conference meeting, and I think that that's not a good place to be. I think every meeting should carry the same amount of weight and attention. And if – and I think this is one way to get that space. So I think that – I think it's a positive development, and I'm going to help him get through those things and manage them as well as he can. (Laughs.)

Q: So, with your comment about the paradox of certainty in mind – (laughter) – is there anything about this three-year overshoot of inflation that is an effort to kind of socialize your idea of symmetry and sort of convince – I mean, we can't switch frameworks because it's too hard to train people to accept higher inflation. Well, aren't you, in fact, kind of doing that now?

MR. BOSTIC: So there are two ways to think about this. On one level, I think an overshoot that is at 2.1, that's not, I don't think, materially different from 2. So I wouldn't read too much into that kind of overshoot as a – as a statement – as a purposeful statement that we're trying to impose symmetry.

That said, I think it's important everybody understand that symmetry is important for us, and it's an important pillar of how we approach the notion of stable prices. And that's important. I think it has – if we don't do that and we're not clear about that, it has the potential to really affect inflation expectations in ways that could make it more difficult for us to achieve our goal.

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* Fed's Bostic Still Sees Three Rate Increases in 2018

Document RSTPROCB20180619ee6j00105

THE WALL STREET JOURNAL.
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REITs, Utilities Lose Luster as Rates Rise

By Michael Wursthorn
790 words
19 June 2018
The Wall Street Journal
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B12
English

The Federal Reserve's hawkish tilt is upending real-estate investment trusts and other stocks with juicy dividend yields that had been thriving in a lower interest-rate environment.

The **S&P 500**'s real-estate sector fell 1.2% last week, hurt by the Fed's decision to lift interest rates on Wednesday and its signal that the bank could pick up the pace of future rate increases.

Those real-estate shares are down 4.5% for the year, among the worst performances of any S&P sector and well below the broader index's gain of 3.7%.

REITs' underperformance is another sign of how the Fed's response to a strengthening economy is rippling through the **stock market**.

Investors often buy shares of real-estate firms and other stocks like utilities for bondlike returns. But as the Fed accelerates the pace of policy tightening, the payouts on U.S. government bonds are rising and forcing investors to consider whether they are better off shifting money into bonds that are poised to see higher yields. The Fed plans to increase rates two more times this year, eventually pushing the fed-funds rate to a range of 3.25% to 3.5% by the end of 2020.

"We're at the point where interest rates are starting to actively compete with high dividend yielding stocks for investors' dollars," said Steven Violin, senior vice president and portfolio manager with F.L. Putnam Investment Management Co., a firm that manages about $1.7 billion in assets.

The yield on the **10**-**year Treasury** note briefly rose above 3% after the Fed's decision Wednesday and continues to hover around that level, settling at 2.926% on Monday. That is just below the 3.1% dividend yield offered by real-estate stocks in the **S&P 500**, which is among the highest in the index.

Wells Fargo & Co. recently downgraded its outlook on the real-estate sector. In a research report, John LaForge, head of real asset strategy at Wells Fargo Investment Institute, said real-estate investment trust "performance often moves in an opposite direction from interest rates."

REITs were also hit hard by the February spike in **10**-**year Treasury** yields.

Real-estate stocks in the **S&P 500** have risen the past four years, when interest rates were at or near zero, and posted a 7.2% gain for 2017.

Wells Fargo says the average REIT trades at a roughly 7% discount to its underlying real-estate holdings, keeping valuations relatively attractive because such investments have averaged a 2.3% premium since 1990. Appealing valuations kept Wells Fargo from downgrading the sector beyond neutral, the bank added in its note.

Commercial real-estate prices have also been gaining, providing some support to the sector amid the changing interest-rate environment. The Green Street Commercial Property Price Index, for example, has steadily risen since 2010.

Fund managers who actively manage portfolios have already cut exposure to the real-estate sector to a six-month low, according to a Bank of America Merrill Lynch report.

Investors pulled $71.8 million in the last week from the Vanguard Real Estate exchange-traded fund, bringing the roughly $30 billion fund's total withdrawals this year to $2.6 billion, according to FactSet.

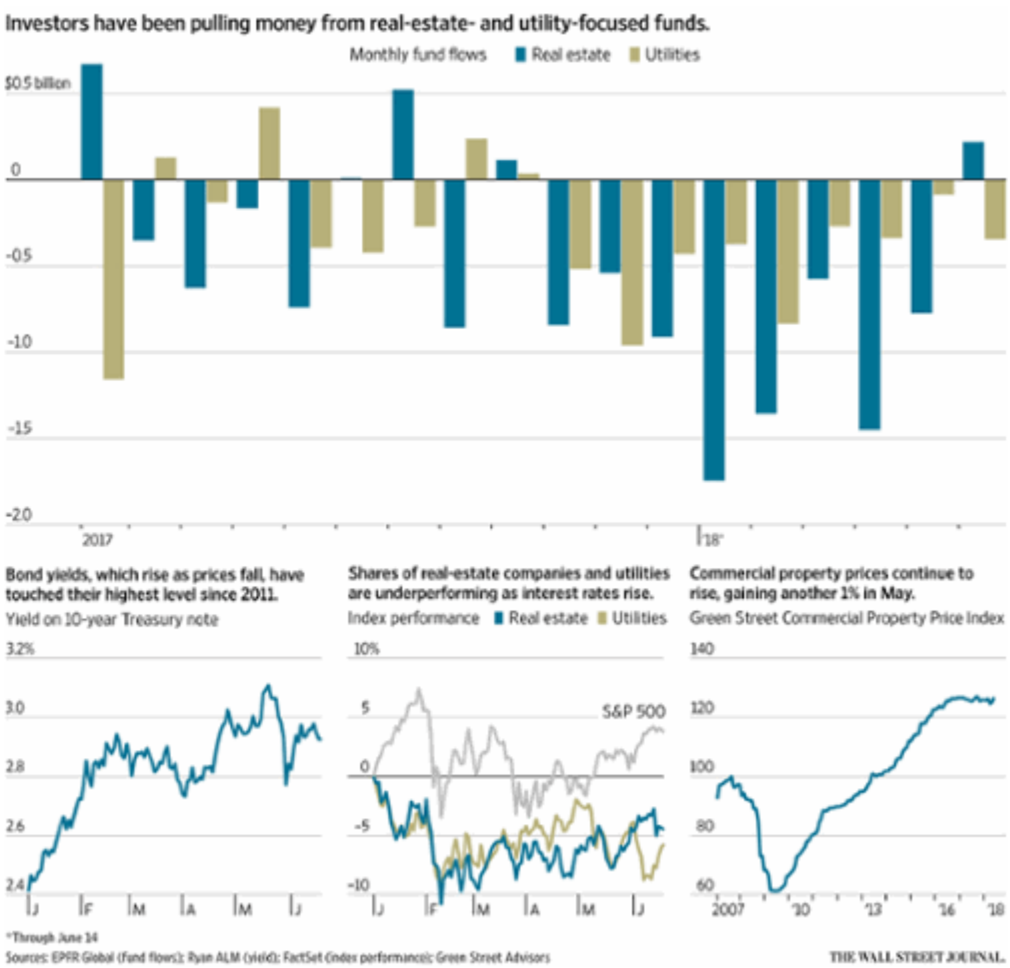
Utility stocks, which also generate hefty dividends and tend to underperform in rising-rate environments, are also struggling, falling 5.7% this year.

Of the 11 major **S&P 500** sectors, active managers have the least exposure to utility and real estate, Bank of America Merrill Lynch said in its report. Utility ETFs managed by State Street Global Advisors, Vanguard Group, BlackRock Inc. and Fidelity Investments have all had withdrawals this year, according to FactSet's data.

Rising interest rates aren't necessarily bad news for stock investors. Shares of financial firms such as banks tend to benefit when interest rates rise because it makes their lending operations more profitable. The KBW **Nasdaq** Bank Index is up 1.1% this year.

Shares of consumer-staple companies, which have struggled lately with trade tensions, rising costs and shifting consumer preferences, are also getting more interest from investors lately. Active fund managers have increased their exposure to the sector for four months running, Bank of America Merrill Lynch said, a defensive posturing in the current environment because those stocks sell everyday essentials like food and beverages that tend to do well in the latter stages of an economic cycle.

Individual investors are taking notice, too, and have contributed to the roughly $219 million that has flowed into the Consumer Staples Select Sector SPDR fund, FactSet said.



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THE WALL STREET JOURNAL.
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Streetwise: There's No Need for Market Tantrum Just Yet

By James Mackintosh
832 words
19 June 2018
The Wall Street Journal
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B1
English

Last week, the Federal Reserve turned hawkish, the European Central Bank said it would soon stop buying bonds and vulnerable emerging markets crumbled. The market narrative is clear: Dollars are getting tighter, and those who loafed about when money was easy will learn what it feels like to have to repay debts.

We last saw something like this in 2013's emerging-market "taper tantrum," which forced several major emerging-market countries to revamp their economies. But despite pain in some big emerging-market currencies, what's happening now isn't the same, at least not yet.

Back then, investors took former Fed Chairman Ben Bernanke's announcement that central-bank bond buying would be tapered as a signal that rate rises were imminent. (They were wrong.) They sent bond yields soaring in preparation for higher interest rates, and currencies of emerging markets reliant on hot-money financing were crushed.

This year is quite different. True, Fed Chairman Jerome Powell was fractionally more hawkish last week than expected and federal-funds futures now put the chance of another two interest-rate rises this year above 50%, according to CME Group. But there has been no sudden leap in long-run expected interest rates, and inflation has been going up just as fast as rates.

In fact, the Fed has been treading water for years, merely raising rates in line with inflation since the start of 2015, on average. This year is on course to be no different. The Fed has raised its forecast for its preferred measure of inflation this year by 0.2 percentage point, and the median forecast of its policy makers for the rate they will set is up by 0.3 point. The gap is little more than a rounding error, and anyway the average private-sector forecast for 2018 consumer price inflation is up by 0.4 point, according to Consensus Economics.

Investors have taken notice, with the 10-year real yield -- from Treasury inflation-protected securities -- only recently returning to its peak in 2013, before falling back. The rise in real yields earlier in the year came well before the emerging-market selloff, unlike in 2013.

The difference matters not only to emerging markets and their investors, but to those trying to understand the dollar and the ECB, too: This time, the economy may be having more effect on markets than the central banks.

Investors wearing rose-tinted spectacles might argue that the emerging-markets selloff is nothing to worry about, really just an unlucky coincidence of local bad news. The currencies of Argentina, Turkey and Brazil have been dumped mainly because of domestic politics, not what is happening at the Fed. The Mexican peso is falling fast, but it is losing because of next month's presidential election and U.S. trade-war fears.

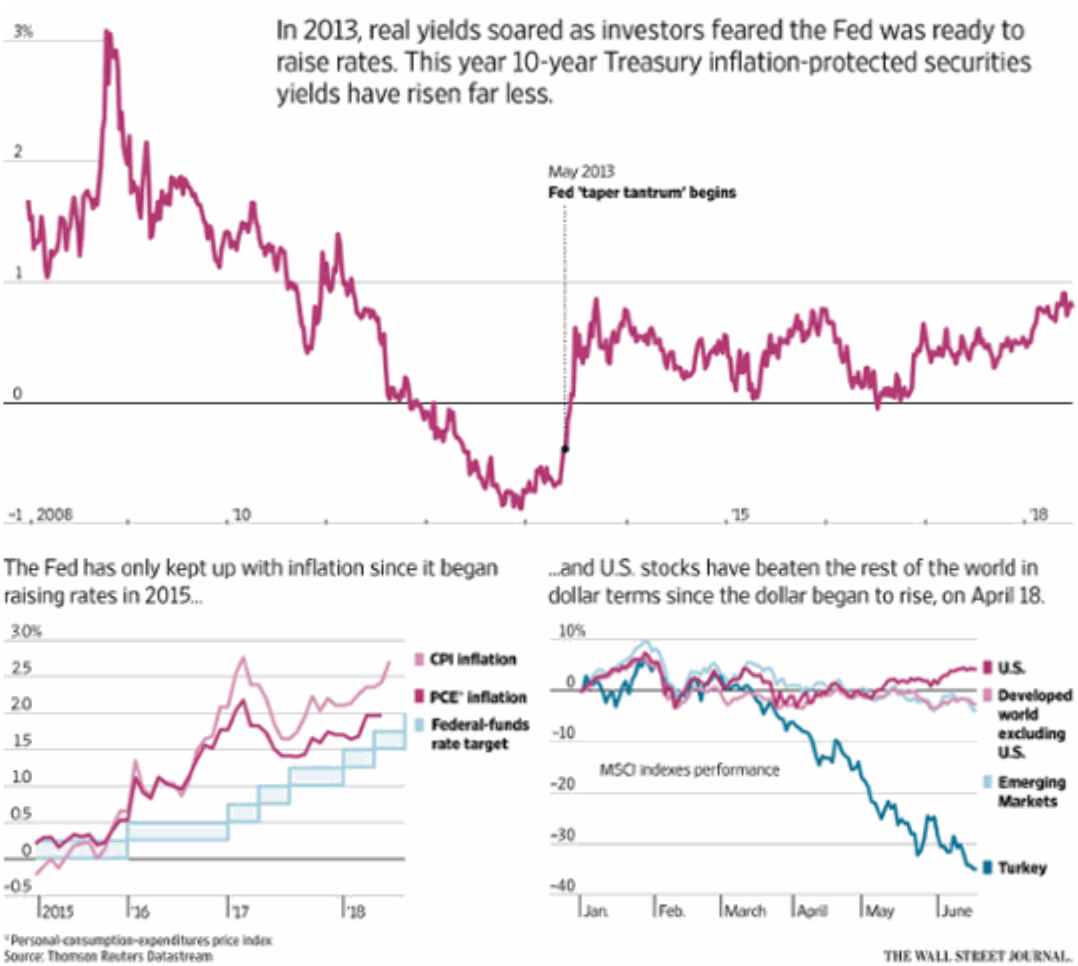
The pessimists will say this is just the start. U.S. inflation has finally reached the Fed goal of 2%, and even "core" inflation, excluding **volatile** energy and food, is very close. Faced with an economy at or close to full capacity, the Fed can shift to worrying about inflation overshooting rather than undershooting, lifting rates above core inflation for the first time since 2009. As real rates rise faster than elsewhere so will the dollar, and emerging currencies will struggle just as they did in every previous dollar bull run.

Both can be right. It is true that the latest emerging currency panic has little in common with the 2013 tantrum. It is equally true that as the Fed moves to positive real rates it might well start to hurt these currencies more broadly.

But at least as important as the central banks this year has been the renewed divergence of the global economy. The U.S. is doing well -- data so far suggest annualized growth in the economy of 4.8% in the second quarter, according to the Atlanta Fed's rather optimistic gauge, and 3% according to the New York Fed's Nowcast -- while the rest of the world has stalled.

The divergence trade is obvious looking back at equities since mid-April, when the dollar started to rally against the euro and other developed markets. U.S. stocks are up 4.3% since, MSCI's dollar-denominated developed world index excluding the U.S. is down 1.8% and the emerging index is down 3.8%.

If the U.S. economy manages to leave the rest of the world in its wake, there could be much more divergence -- during the 2013 taper tantrum U.S. stocks beat emerging-market stocks by 20 percentage points. But investor expectations are already pretty low for much of the emerging world and for Europe, and pretty high in the U.S. It wouldn't take much sign of renewed synchronization to halt the dollar's ascent and the divergence trade.



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THE WALL STREET JOURNAL.

Markets

Trade Tensions Pinch U.S. Yield Curve; Investors use yield curve as a guide to economy's direction

By Daniel Kruger and Orla McCaffrey
619 words
19 June 2018
02:16 PM
The Wall Street Journal Online
WSJO
English

The gap between yields on short and longer-term U.S. government debt narrowed Tuesday to its smallest in almost 11 years as trade tensions between the U.S. and China intensified.

The spread between the yields on two- and 10-year Treasurys, known as the yield curve, flattened to 0.358 percentage point, the smallest since August 2007, according to data from Ryan ALM.

Investors and economists look to the measure as a guide to the direction of the economy, with steeper yield curves signaling stronger growth. Two-year yields have risen above 10-year yields in each U.S. recession since at least 1975, a phenomenon known as an inverted yield curve.

Tuesday's move was fueled by a rally in longer-term U.S. government debt after President Donald Trump intensified a trade dispute with China, threatening tariffs on $200 billion of imports after China retaliated against an earlier round of U.S. trade levies.

The new tariff threats raised questions about how well investors expect the economy to weather rising trade tensions. Investors and analysts cite the potential for tariffs to slow economic growth and curb the pace of employment gains.

Trade tensions have been a major focus for investors this year. But the latest escalation suggests that many have underestimated the willingness of the world's two largest economies to retaliate against one another, analysts said.

Rather than de-escalating, some analysts predict the situation will worsen—stoking further market **volatility**—in the run-up to the implementation of an earlier round of U.S. tariffs, on July 6.

"I don't think investors are quite concerned yet" about the risk of a recession, said Justin Lederer, a government bond strategist at Cantor Fitzgerald LP. However, "things can change very quickly with trade wars going on right now. It has an impact on the [U.S.] economy, and on the global economy."

The continued flattening of the curve has been spurred by expectations the Federal Reserve will continue to raise interest rates, which have pushed the two-year yield higher. Fed-funds futures early Tuesday indicated that the odds the Fed will raise interest rates four or more times this year were at 51% early Tuesday, down from 55% Monday, according to data from CME Group.

At the same time, the yield on the 10-year note, which is more sensitive to expectations for growth and inflation, has retreated from its push above 3% earlier this year. The 10-year note yield eclipsed 3% in April for the first time since January 2014, soaring amid hopes that tax cuts would boost growth and inflation to a recent peak of 3.109% on May 17.

Analysts said many investors failed to expect the Trump administration's focus on trade after the passage of tax cuts and are adjusting to a new set of expectations.

"The market's not reacting to uncertainty; it's well past that," said Jim Vogel, head of government bond strategy at FTN Financial. "The market understands well what the White House trade policy is. The bond market is fed up with the topic."

Write to Daniel Kruger at Daniel.Kruger@wsj.com

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WSJ PRO CENTRAL BANKING

Markets

Global Under-Supply of Oil in Coming Years, Dallas Fed Says; Report says low crude prices prompted producers to cut back

By Dan Molinski
600 words
19 June 2018
10:00 AM
WSJ Pro Central Banking
RSTPROCB
English

DALLAS—Oil prices could rise more in the years ahead as global supply begins to lag ever-growing demand, but a strong U.S. economy should be able to handle the higher prices, the Federal Reserve Bank of Dallas said in a report released Tuesday.

While higher oil prices—which last month reached a three-year high above $70-a-barrel—create pass-on inflationary effects on prices for gasoline and other goods that have proven quite harmful to the U.S. economy, the Dallas Fed said it believes America's always-evolving economy is better-built now.

"Historically, recessions in the U.S. have often followed oil price shocks," said the report, Perspectives in Oil, authored by Dallas Fed President Robert Kaplan. "Higher oil prices tend to increase costs to consumers, which can, in turn, reduce their disposable income and consumption of non-oil goods and services."

But the explosion of domestically-produced oil from shale has the U.S. now producing about 11 million barrels a day of crude oil, double the rate from 2011. This has created tens of thousands of new jobs in drilling, oil-field services, trucking, shipping and other sectors, and that "means that a larger share of the economy is helped by higher oil prices," the report said.

Beyond that, the Dallas Fed said the U.S. economy is less oil-intensive than in the past due to substitution for oil by other forms of energy, improved fuel efficiency and growth in economic sectors that are less energy-intensive compared, say, to an economic landscape dominated by old, power-hungry manufacturing plants.

"It is the view of Dallas Fed economists that the negative impact of higher oil prices on gross domestic product growth is likely to be more muted than in the past," it said. "It is our view that a 10% increase in the oil price should have a relatively modest negative impact on U.S. GDP growth."

The report didn't say how exactly high the Dallas Fed thinks oil prices may ultimately reach, though it said supply and demand for oil, which it believes is roughly in balance right now, could eventually shift significantly to an undersupply situation.

The collapse in oil prices in late 2014 led oil companies around the world to reduce investment spending on deepwater, ultra-deepwater, arctic drilling, oil sands drilling, and other projects that typically cost hundreds of millions to billions of dollars to complete, but are vital to longer-term global oil-supply needs, it said.

That drop in spending could thus mean a supply shortfall ahead, the Dallas Fed said, noting also that there are growing impediments to continued growth in U.S. shale production due to factors such as labor shortages, and environmental and infrastructure challenges.

Meantime, global demand for oil grew from an average of 90.4 million barrels per day in 2012 to approximately 98.4 million barrels per day in the first quarter of 2018, and could hit 101.5 million by 2020, it said, led by demand growth from emerging economies like China and India.

This eventual supply-and-demand imbalance could also make oil markets more sensitive to disruptions from oil-producing, politically-unstable areas of the world such as Venezuela and Libya, making the overall oil market "more vulnerable to geopolitical events and other dynamics that could create price risks to the upside."

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THE WALL STREET JOURNAL.

Economy

Draghi Says ECB Could Restart Bond Buying-Program If Required; Comments from central bank chief underline caution in winding down stimulus program

By Tom Fairless
797 words
19 June 2018
10:29 AM
The Wall Street Journal Online
WSJO
English

SINTRA, Portugal—European Central Bank President Mario Draghi signaled Tuesday that the bank could delay plans announced just last week to end its giant bond-buying program, underlining policy makers' caution in phasing out easy money as the region's economy slows and faces new risks.

Mr. Draghi's comments highlight a growing policy gap between the world's top two central banks: The Federal Reserve last week raised short-term interest rates and signaled two more rate increases this year to stop the U.S. economy from overheating, even as the ECB signaled it wouldn't raise rates before next September.

Speaking at an economic conference in Sintra, Portugal, Mr. Draghi suggested investors might need to wait even longer for a first interest-rate increase from the ECB, and that any policy moves after that would be gradual.

The comments come just five days after the ECB announced plans to phase out its €30 billion a month bond-buying program by the end of the year, even as it holds interest rates below zero "through next summer."

Those plans are "subject to incoming data confirming the medium-term inflation outlook," Mr. Draghi said Tuesday. The bank's €2.5 trillion ($2.9 trillion) bond-buying program "can always be used in case contingencies materialize that we do not currently foresee," he said.

The shift in tone—which helped push the euro down about half a cent to $1.15, roughly the same level as a year ago—underscores the changing economic fortunes of the 19-nation currency bloc, whose growth rate has roughly halved over the past year to an annualized 1.6%. The euro had surged as high as $1.25 earlier this year.

While ECB officials are eager to phase out the bank's bond purchases, known as quantitative easing, they are concerned about mitigating the impact on the region's weakening economy. Analysts doubt that the ECB could extend its bond purchases for much longer without violating self-imposed rules designed to stop the bank from financing governments or overly distorting market prices.

Mr. Draghi highlighted a series of threats to the region's economy Tuesday, ranging from trade conflicts to rising **oil prices** and **financial-market volatility**. He stressed that the ECB's key interest rate—currently minus 0.4%—wouldn't rise at least through the summer of 2019, and perhaps beyond that.

"What is undeniable is that uncertainty surrounding the growth outlook has recently increased," Mr. Draghi said.

The comments, at a conference that is the ECB's answer to the Fed's annual economic symposium in Jackson Hole, Wyo, come a year after Mr. Draghi signaled at the same event that the ECB could soon phase out easy money. That speech, seen as marking a new policy convergence between the ECB and the Fed, led to a protracted appreciation of the euro.

The outlook for the eurozone economy has since darkened considerably even as the U.S. economy has powered ahead. Mounting trade tensions between the U.S. and China could disproportionately hit the 19-nation eurozone because of its heavy focus on exports. The U.S. economy is also insulated from higher **oil prices** thanks to surging domestic oil production.

Investors are cautiously eyeing the actions of Italy's new populist government, and even Germany faces political uncertainty as Chancellor Angela Merkel seeks to fend off a rebellion from a junior coalition partner over migration.

Germany's central bank Friday slashed its growth forecast for the largest eurozone economy this year and said concerns over protectionism and "greater political uncertainty in some euro area countries" had clouded the outlook. The Bundesbank now expects growth of 2% this year, down from a forecast of 2.5% in December.

In the face of those risks, Mr. Draghi stressed that the world's number two central bank will remain "patient, persistent and prudent."

"Our decisions also reflected the desire of the Governing Council to retain the ability to react to potential future shocks," he said.

After years of easy-money policies, some analysts and officials worry that major central banks have little ammunition left to deal with any fresh economic downturn.

Speaking in Sintra on Monday evening, former U.S. Treasury Secretary Lawrence Summers said central banks had traditionally fought recessions by cutting interest rates by around 5 percentage points. Yet both the ECB and the Federal Reserve are likely to have "nowhere near" enough space to do that for many years, Mr. Summers said.

"The world can ill afford an economic downturn," Mr. Summers said.

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WSJ PRO CENTRAL BANKING

Economy

Bullard: Successful Inflation-Fighting Measures By Central Banks Have Flattened Phillips Curve; St. Louis Fed president didn't address economic outlook or timing of Fed rate increases

By David Harrison
360 words
19 June 2018
08:02 AM
WSJ Pro Central Banking
RSTPROCB
English

Central bankers have gotten so good at containing inflation over the past 30 years that they have obscured the link between inflation and unemployment, Federal Reserve Bank of St. Louis President James Bullard said Tuesday.

In a presentation prepared for a conference in Portugal, Mr. Bullard said central banks reacted so strongly and effectively to bring down inflation in the 1970s and 1980s that inflation has since become less **volatile**. That means periods of low unemployment, such as the one currently under way, are unlikely to push it up, he said.

"Ultimately, successful monetary policy can push the empirical Phillips curve slope all the way to zero," he said.

The relationship between inflation and unemployment, known as the Phillips curve, underlies much of central banking's economic analysis. The idea is that when unemployment falls below a certain level, it will trigger wage gains and price increases.

But unemployment in the U.S. has been drifting down since the recession and now stands at 3.8%, the lowest level in 18 years. Meanwhile, inflation pressures have been muted. Inflation has run below the Fed's 2% target for much of the past six years although it has picked up in recent months.

Fed Chairman Jerome Powell last week described the fact that wages haven't risen despite the fall in unemployment as "a bit of a puzzle."

Mr. Bullard said central bankers should stop relying on the Phillips curve to set policy. That suggests letting unemployment fall even lower might not trigger the run-up in inflation that some of Mr. Bullard's colleagues have warned about.

The St. Louis chief has been one of the central bank's more vocal advocates for patience in raising interest rates.

"Today's G-7 monetary policy makers are unlikely to glean a reliable signal for monetary policy based on empirical Phillips curve slope estimates—they have to look elsewhere," he said.

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Advertising (A Special Report) --- What's an Online Ad Worth? Blockchain May Help With That

By Henry Williams
1,139 words
19 June 2018
The Wall Street Journal
J
R8
English

Digital advertising has a serious problem: fraud.

Widespread fraudulent practices are inflating measures of the traffic that digital ads attract, leading some advertisers to pay higher rates than they should.

Can blockchain fix it?

A handful of blockchain startups believe so. They argue that a shared digital ledger to authenticate and safeguard advertising data, a transparent exchange for trading digital ads, and a special ad-focused browser that pays its users in tokens could each help fix that multibillion-dollar problem.

The industry standard for gauging how much an online ad is worth is the so-called CPM, short for cost per 1,000 views. Less honest players in the industry, however, seek to boost these numbers using bots and other methods that make specific digital ads or ad positioning opportunities appear as if they are getting more traffic than they really are, thus inflating their value.

Juniper Research put the cost of fraud at $14 billion in 2017, and predicts it will grow to $19 billion this year. Some 16% of global ad click-throughs are fraudulent, according to Juniper. Industry estimates of the number of fraudulent click-throughs conflict, however, and that's part of the problem, too. There are no standards in the industry for digital-ad data sharing, and there is no common exchange where transactions among advertisers, brokers and Web publishers can take place. It is hard to track data reliably.

Enter MetaX, a digital advertising startup based in Santa Monica, Calif.

"With so many discrepancies, it's hard to trust the numbers that everyone is sharing," says Chief Executive Ken Brook. "Numbers are being deliberately modified or skewed. . .to get paid more."

MetaX is building up a user-driven registry of trusted advertisers and publishers it calls adChain, which verifies that the advertiser and publisher behind ads are legitimate. Members of adChain, which so far include Facebook Inc., Pandora Media Inc. and Hearst Corp., buy their memberships using a crypto-token called adToken. They also get to decide who belongs in the registry with them. Members put a stake down if they want to vote a member out, and the winner of the challenge takes the stake. Mr. Brook says that challenging new members is a way for the community to actively create trust.

"We encourage active voting. . .and participation in the curation process," he says. "Just because you're in the registry doesn't guarantee you'll stay in the registry for long."

The current cost to entry is 1,500 tokens (current exchange rates would value this at about $30). MetaX hopes that with the community acting as gatekeepers to new applicants, it will create a high-quality list of reputable sites. There are currently about 50 members.

Mr. Brook hopes the system will encourage trust in ads in a similar way to the green "padlocks" that denote security for banking and e-commerce sites.

It is still facing some growing pains, though, as members get used to the system. For example, members of the registry have suggested that well-known sites like Spotify.com don't belong in the registry. Others have submitted their own personal sites for membership in an effort to create publicity for their websites, while never intending to show ads.

The CEO of MetaX says the company is working on a "constitution" that will make the rules clearer about what kind of sites belong in the registry.

Another blockchain startup that sees a big opportunity in fixing the digital advertising market is NYIAX, a New York-based company that has built an exchange for trading advertising contracts in partnership with **Nasdaq**.

"We wanted to create a language on top of [**Nasdaq** OMX's exchange technology] so that it can understand advertising as if it were a financial instrument," says Carolina Abenante, the founder of NYIAX.

The exchange, which expects to go live in July, will have Web publishers and advertisers posting requests for contracts, bids, and the details of completed contracts and fund transfers -- like a traditional financial exchange. By maintaining all of the details on the blockchain ledger, NYIAX says it can give full transparency to the counterparties trading through its system, verifying that ads appear in the positions promised and draw the traffic that they claim.

In addition to providing transparency, the exchange hopes to create a kind of futures market for advertising, giving publishers the opportunity to lock in the income from advertising ahead of time. It is similar to how an airline might purchase contracts to buy jet fuel ahead of time to guarantee the price they pay. Advertisers get the benefit of having publishers ready ahead of time, allowing for planning in their ad development.

Attempts by the blockchain startups at gaining a foothold in the well-established ad industry face two significant challenges -- Facebook and Google. Together, the two ad giants captured 74% of the digital ad market in 2017, according to Pivotal Research Group. And both companies have been working on solving the problem of ad fraud. Google, for its part, has rolled out the Ads.txt industry initiative, an attempt to prevent counterfeit online ad space.

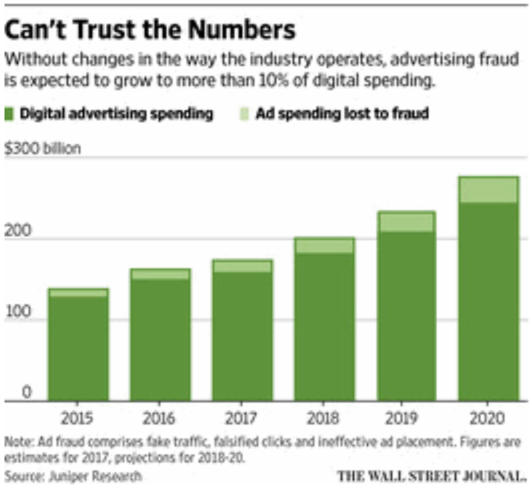
Still, a third blockchain-related startup, Brave, tries to address lack of trust in online ads as well. At the center of Brave's business plan is a special browser that blocks ads users don't want to see and rewards them for looking at ads that they do want to see. A blockchain application that is also part of the system will verify how much attention each ad receives and subsequently reward both the advertiser and the consumers who look at the ad.

Brave Founder Brendan Eich, creator of the widely used JavaScript website software, says that while consumers are used to seeing Google and Facebook use their data to figure out their ad preferences, Brave processes users' data on the browser without sending it over the internet. Users' interactions with ads are then anonymously synced up with the blockchain once a month.

The plan also calls for a cryptocurrency-like coin the company calls the Basic Attention Token, or BAT, to be used as payment between advertisers and publishers. Consumers who look at ads also will receive BATs, which they will be able to use on the Brave platform to buy games or gift cards, or donate to sites or other advertisers they like. While consumers won't be able to convert their BATs into cash, Web publishers will, through a third party.

The company expects the system to be fully operational this summer.

Mr. Williams is a deputy editor for The Wall Street Journal in New York. Email henry.williams@wsj.com.



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U.S. News: Modest Earners Gain Confidence

By Sarah Chaney
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Economic confidence among lower-income Americans has taken a recent leap, the latest evidence that benefits of the economic expansion are reaching a broader group of workers.

Sentiment among lower-income consumers still trails that of their higher-earning counterparts, but the gap has narrowed in recent months.

In the University of Michigan's consumer-sentiment index, confidence among households in the bottom-third income tier has risen 11.4 points since February, an IHS Markit analysis of sentiment figures shows. Meanwhile, sentiment among Americans in the highest third of incomes has fallen more than 8 points.

The recent improvement in confidence for lower-income Americans coincides with a falling unemployment rate and faster wage growth for workers at the margin. Among those experiencing labor-market gains are the less educated and African-Americans, who trailed behind other groups for much of the economic expansion beginning in mid-2009.

A tightening labor market and increased take-home pay from the tax cut passed in December are likely translating into renewed confidence among lower-income Americans. These factors outweigh any decreased confidence stemming from a rise in gas-pump prices, said Chris Christopher, IHS Markit executive director.

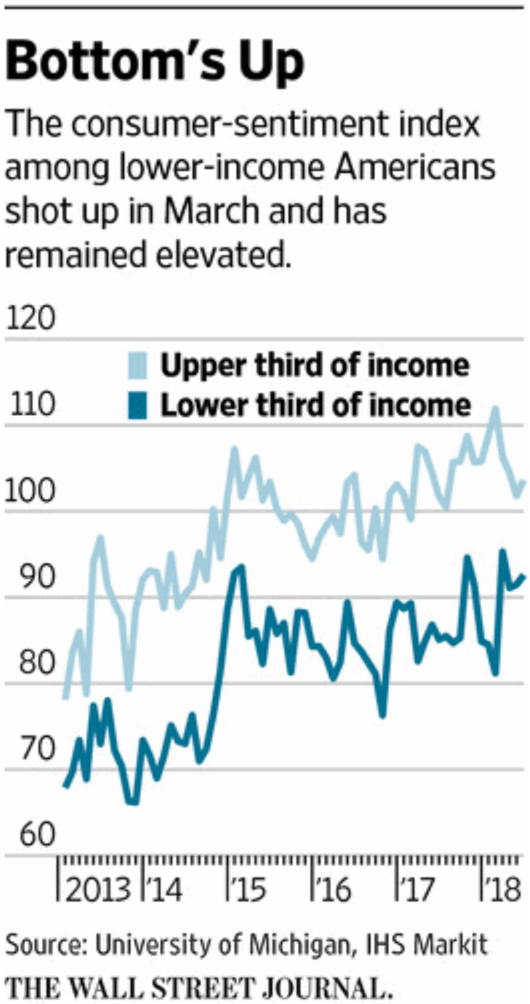
"You say to a lower-income person. . .'Hey, you have [an] extra $50, $100 a month, that really makes a big difference. With that, they'll go out to eat more," Mr. Christopher said.

Confidence among higher-income Americans has taken a hit because of recent **stock-market volatility** and concerns about possible trade wars, Mr. Christopher said.

Overall consumer sentiment rose after the election of President Donald Trump and has remained strong. The University of Michigan on Friday said its preliminary reading on consumer sentiment in June rose, propelled by Americans' greater optimism toward the economic situation.

The IHS Markit analysis of the sentiment data shows confidence has fallen about 7 points among households with incomes of more than $75,000 since February. Over the period, optimism has risen 8 points for households with incomes of less than $75,000, so the gap in confidence between these two income groups is the narrowest since December 2015.

The jobless rates for African-American and Latino workers are near record lows. The jobless rate for those without a high-school diploma touched a 25-year low late last year and has held below 6% this year.



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