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Hinds Financial Group Quarterly Economic Outlook and Review Q2 2018

The Economy

The US economy remained on an uptrend, although growth in the first quarter was the lowest in a year. The employment situation continued to post gains, with an average of approximately 179,000 jobs added each month. At the same time, the unemployment rate fell to 3.8%. The Federal Open Market Committee (Fed) modified its interest rate policy by raising the federal funds rate target 25 basis points to a range of 1.75% to 2.00%. Economists expect up to two additional increases in 2018, as economic growth accelerates and inflation and wage pressures increase.

Domestic Stocks

Equity markets moved modestly higher during the quarter, seeming to take two steps forward and one step back. The volatility appeared to be a result of investor angst over the Trump Administration's trade policy and its insistence on imposing tariffs on certain imported goods. Markets generally do not like tariffs, considering them to be a tax. In addition, our trade partners have not shrunk from the fight, retaliating with their own tariffs on goods that we export. These escalating tensions create uncertainty in the minds of investors, who are beginning to wonder if the benefits of the tax cuts will be offset by the adverse effects of the trade war. Within this landscape, the S&P 500 Index finished the quarter with a modest gain of 3.4%.

International Stocks

International stocks performed poorly on a relative basis, with almost all markets lagging US equities. Economic growth, although still positive in most regions, cooled in the second quarter. As a result, international stock indices had a difficult time. The MSCI ACWI Ex-USA Index, which measures performance of world markets outside the US, declined 2.6%.

Bonds

Several factors affected fixed income securities' prices and yields, including the Fed's decision to raise short-term interest rates once again at its recent June meeting; the escalating rhetoric with China and other trading partners regarding trade and tariffs; and geopolitical events, such as President Trump's summit with North Korea leader, Kim Jong Un. The President's continued strong stance on trade has disrupted financial markets, but the fixed income market has largely moved to the tune of the economy's resilient growth. The benefits of an aggressive fiscal policy, including the tax cuts signed into law in the past six months, are now beginning to flow through the economy, and the Fed is taking a measured approach to raising interest rates to mitigate any overheating. The Fed expects to raise short-term rates at least two more times in 2018.

Outlook

The US economy remains strong, and although the current expansion is now the second longest in history, the consensus among economists is that the prospects for further growth are solid. Aggressive fiscal stimulus in the form of deficit-financed tax cuts and increased government spending, according to many economists, has the potential to provide the fuel for continued expansion for at least the next several quarters. We believe these factors could accelerate domestic economic growth in the short term. Not all is bright on the horizon, however. The escalation in trade skirmishes poses a real threat to this growth, as investors view tariffs as tax increases, because consumers will spend more on imported goods. If the tariff retaliation were to end with what has already been imposed, leading economic consulting firm Moody's Analytics projects that the overall effect would not be significant. However, if the additional tariffs that have been threatened—and their retaliatory responses—are imposed, Moody's estimates an adverse impact on GDP. For that reason, if the brinksmanship doesn't subside, there is a real possibility of a tariff-induced recession down the road. But the expectation is that if the equity market continues to have difficulties as a result of the back-and-forth tariff tiff, President Trump will relent, enabling the recent strong growth and employment gains to continue.