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TPWC Market and Economic Update

The Markets

The U.S. stock market, represented by the S&P 500 Stock Index (SPX), turned in a respectable 1.99% gain for the week, closing at 2656.30. That still leaves it down 0.65% year-to-date, but up an impressive 14.06% from this time last year. Early in the week and again on Friday the SPX dipped on trade-war tweets, but in the end, it was solid earnings reports from financial companies that saved the day (week). Another upbeat item was the rise in oil prices, which translates into higher expected earnings for energy companies.

U.S. Crude oil futures for May delivery hit $67.39, up 8.6% for the week as tensions escalated in the Middle East. Gold rose 0.84% for the week and is up 3% for one year at $1,348.60. The 10-year U.S. Treasury note resumed its slow rise to close at 2.825% in the mid-range of recent yields. As a side note, Bitcoin, the wunderkind of speculators at the end of last year as it rose to nearly $20,000 was down into the $6-7 thousand range for the week, having lost nearly 70% year to date.

The Economy

One of the indicators that an economy is rapidly growing and may be reaching its limits can be seen in the transportation industry. Currently, just about all the long-haul 18-wheelers that are available are filled and their drivers are pushing the legal limits of time behind the wheel. Trucking companies ordered 139,900 heavy-duty trucks in the first quarter, nearly double the number from last year according to analyst group FTR. The group also reported that trucking companies are seeing a substantial number of orders above that which they can carry and are starting to charge premium fees in some cases.

In the first quarter, the number of truckloads of freight ready to move rose 27% while the number of rigs available rose only 14%. The negative to this good news is that increased transportation costs tend to get passed along creating higher prices, which creates inflationary pressures. While the rigs are in short supply, the drivers are already at 100% utilization, up from 85% three months ago. To get more drivers, higher wages will be required. The economy has hit its first bottleneck. It is in the bottlenecks where inflationary forces are brewed.

That bottleneck contributed to a rise in core inflation to a 2.9% annualized rate in the first quarter as measured by the Consumer Price Index (CPI). The Federal Reserve's favorite measure, the Personal Consumption Expenditures Index (PCE) is now running at an annual rate of about 2.5%. Since the Fed has a target inflation rate of 2%, interest rates are likely headed up to slow the economy. Meanwhile, producer prices rose at a 3.6% annualized rate in March after increasing 3% from this time last year; another indicator of building inflationary pressure.

In an odd twist of events, as we reported last week, the aluminum tariffs targeted at China actually reduced the price of aluminum, but aluminum prices then jumped about 25% and alumina, the raw material, rose 30% as the administration imposed trade sanctions on Rusal, the Russian company that supplies about 7% of the world's aluminum and alumina.

The Congressional Budget Office (CBO) announced that the federal deficit will hit at least $1 trillion dollars starting in 2020. The forecast included a warning that the interest payments on that debt will exceed the Defense budget by 2023 and become larger than all federal discretionary spending by 2025. The CBO also predicted that the U.S. economy would likely grow 3.3% for 2018 but then decline to 2.4% in 2019 and average 1.7% in 2023 and later. It appears more and more that the 2017 tax cut bill will boost economic growth in 2018 while generating a rise in inflation, at the expense of higher debt and a slower economy in the follow-on years.

The bottom line continues to be that the economy is in excellent shape with corporate earnings on track to continued growth. In the short term, the wild card remains trade tariffs. If the President's announced tariffs and China's counter-tariffs go into effect, those earnings estimates will need to be recalculated and with them the potential market gains. Longer-term, the combination of increased federal spending and revenue reductions may take us into a slump in late 2019 and for 2020. Stay tuned.

Until next week, we remain your faithful servants,

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