Weekly Market Insights

July 8, 2019

Markets advance, employment rebounds and congratulations Christine Lagarde!

Equity markets had another good week. The Dow Jones Industrials rose 1.2%, the S&P 500 was up 0.54% and NASDAQ rose 1.94%. The gains were predominantly due to investors' expectations that the Fed would lower interest rates. The belief in the Fed easing started to take on mythical proportions, with some analysts suggesting that the Fed would lower interest rates 50 bps (basis points) in July.

The Department of Labor announced the economy created 224,000 new jobs last month. The expectations were for an increase of 160,000. That number, 224,000, is not the greatest but it was much higher than expected and showed a substantial reversal of the anemic job growth last month. Interestingly, the unemployment number rose and that is good news. It went up not because of an increase in the jobless rate, but because more people are entering the work force, which is something the American economy badly needs. Perhaps it is a good time to remind readers that economic statistics are prone to revision, so analysts must be careful not to make too much of a release that strays from expectations.

An interesting point is that market participants had an option of how to analyze the revision. The first is a negative view: Darn, the economy is stronger than expected and not heading to recession, or the positive view: Great, the economy is stronger than expected and not headed toward a recession. It will be interesting to see how the next set of economic releases reads.

Europe, in the meantime can't seem to break out of the economic doldrums. The EU economy is stuck in a torpor and there doesn't seem to be anything in the near horizon to help.

The latest dismal statistic comes from Germany where factory orders plunged. It shook investors, but it should not have been a particularly stunning surprise. Germany has certainly been the economic powerhouse of the European Union. It is interesting to take a close look at the German economy for clues as to why investors may have expected this. Germany has been the most powerful export nation in all of Europe and they also are the thriftiest keeping domestic spending down. Germany has also been helped dramatically by the Euro, a common currency that has been kept low because of the economically weak nations of the EU. This has been great for Germany but not for the weaker countries. When the tariff wars began and international trade began to falter, Germany's exports fell, just as in all countries. The German problem is a version of the "Paradox of Thrift." If one person saves a lot, it is a positive thing and if everyone saves a lot, it reduces aggregate demand and slows a nation's economic growth. Germany's aggressive savings rate does not allow for an expansion of domestic demand to compensate for the reduction of exports.

A positive note from Europe is the nomination of Christine Lagarde as the President of The European Central Bank (ECB). Ms. Lagarde is highly qualified. She spent years as a successful Finance Minister of France and most recently served as head of the International Monetary Fund (IMF). She has great management skills and is very bright. However, the naysayers' complaint is twofold. Some will say how can she be head of the ECB and not be an economist? Easy, she will have some of the finest economic minds to advise her. A good example is Jerome Powell, Chairman of the U.S. Federal Reserve. Mr. Powell, just as Ms. Lagarde, is a lawyer, a good listener and manager and is doing just fine. The other complaint, which probably will be lodged by the Germans, is that she will almost certainly be an advocate of easy money. I say that with great confidence because I was fortunate to have heard her concerns about the EU economy during a conversation at a World Bank/IMF conference this past winter. She will make a very fine ECB president.

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