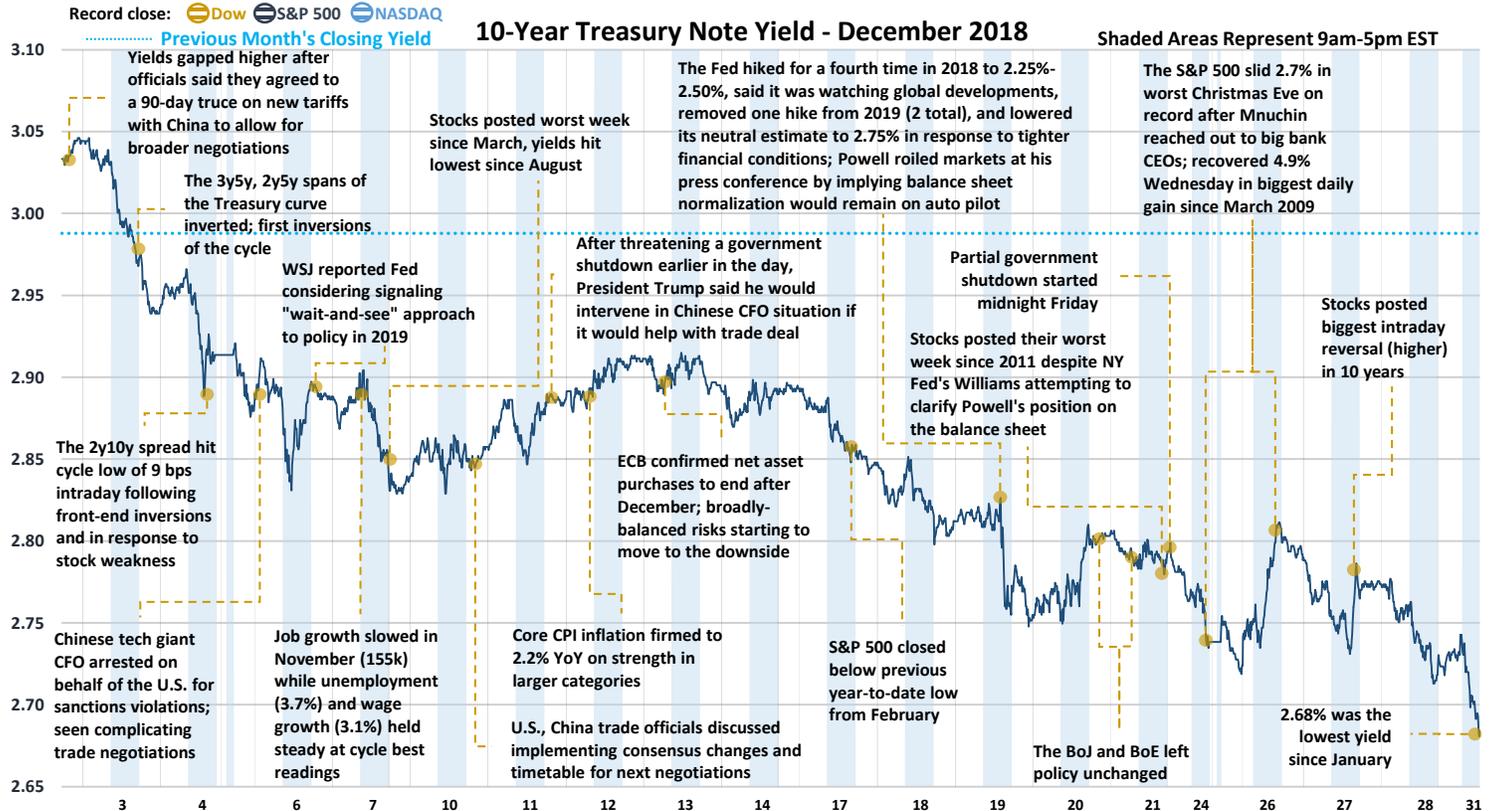


# Monthly Review

December 2018

Yields Tumbled as Growing Uncertainty Handed U.S. Stocks Their Worst December Since the Great Depression



## Concerns the Fed is Too Cavalier Towards Uncertainty around Trade and Global Growth, a Curve Inversion, and Recent Market Volatility Roiled Markets in December

**Markets:** December was historic for the stock market amid growing uncertainties around trade and global growth, Treasury curve inversions, concerns the Fed is tightening too aggressively, and a partial government shutdown. The S&P 500 fell 9.2% in its worst December since the Great Depression (1931), the first time in history a December has registered as the worst month of a year. December's plunge pushed the index down 6.2% for the year, its worst annual performance since 2008, and into a 14.5% correction from its September peak. The U.S. and China agreed to hold off on any new tariffs until March but subsequent events kept uncertainty elevated. The 3y5y and 2y5y became the first spans of the Treasury curve to invert since the Great Recession as the Fed hiked for a fourth time in 2018. They did lower their forward expected path but Chairman Powell didn't sound as dovish as markets would have liked. Still, Fed Funds futures ended essentially pricing out any additional rate increases during this cycle. In response, the 2-year Treasury yield fell 30 bps to 2.49%, the lowest since early June. Both the 5-year and 10-year yields slid 30 bps, the 5-year yield to 2.51% (lowest since early February), and the 10-year yield to 2.68% (lowest since January). Oil prices sank 10.8% and WTI ended down 41% from its early October peak.

**Consumer:** November's retail sales blew out estimates and included sharp positive revisions for October. The positive implications were consistent with anecdotal evidence from several large U.S. retailers reporting robust holiday sales activity. Job growth slowed but remained solid in November while unemployment and wage growth held at their best levels of the cycle. And while the continued strength of the labor market was acknowledged by consumers who responded to the Conference Board's December confidence survey, growing uncertainty about the future pulled overall sentiment down to its weakest level in five months and future expectations to a 25-month low.

**Private Investment:** Positive revisions to October's capital goods orders didn't fully offset November's weakness, leaving the outlook for business equipment spending modestly weaker than expected. While both ISM reports topped estimates, the latest regional Fed surveys disappointed and small business optimism fell to an eight-month low. The most recent new home sales data was postponed because of the government shutdown but disappointing builder confidence and single family starts and permits were consistent with continued softening. Another monthly decline in pending sales raised questions about the sustainability of a second month of stronger existing home sales and slower price gains continued with the S&P Case-Shiller YoY 20-City Composite down for a seventh month in November to its weakest since October 2016.

**External Trade:** After dragging 2%-points from 3Q growth, the October trade deficit hit (\$55.5B), the widest since 2008, as the U.S. economy continued to outperform other major global economies and the U.S. and China remain locked in a trade scuffle.

**Inflation:** Both Core CPI and PCE inflation firmed up in November as expected but modest monthly gains continued to create little fear that undue inflation pressures are building. In fact, another month of lower oil prices and a strong Dollar sent 5-year TIPS inflation expectations to close at 1.49%, the lowest level since October 2016.

**Monetary Policy:** Despite growing uncertainties and heightened market volatility, the Fed raised rates for a fourth time during 2018 to a range of 2.25% to 2.50%. They did, however, add a line to the Statement that they would "monitor global economic and financial developments" and softened the "further gradual increases" they expect by adding a "some" in front. That was consistent with moderating tweaks to the economic projections and a lower projected path in the dot plot; two 2019 hikes instead of three and a 0.25% cut in the neutral estimate to 2.75%. But Powell roiled markets when he said balance sheet normalization was running smoothly and likely to remain on autopilot, interpreted by the markets as a signal rate hikes were data dependent but the balance sheet plans were not.

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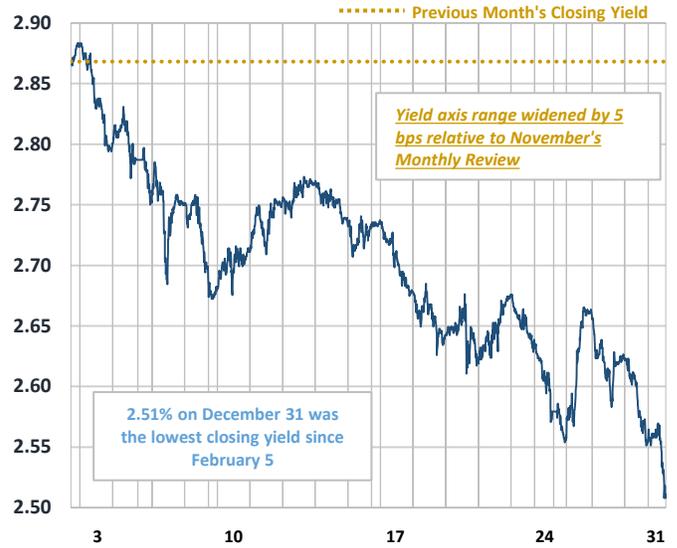
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2-Year Treasury Note Yield - December 2018



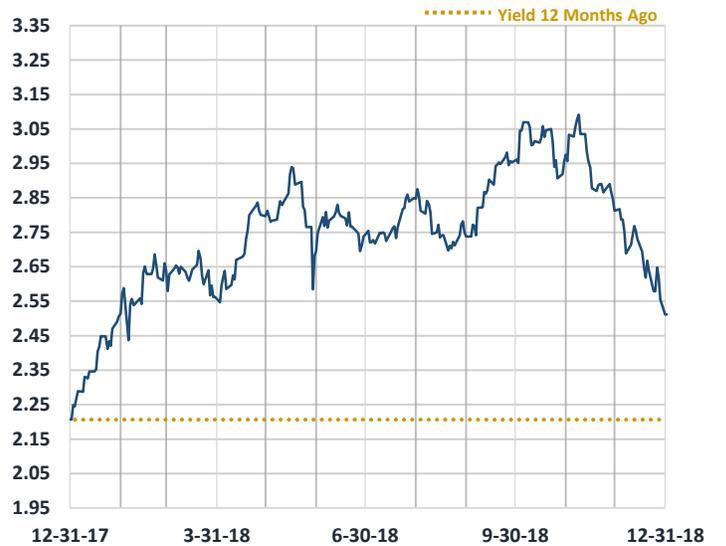
5-Year Treasury Note Yield - December 2018



2-Year Treasury Note Yield - Last 12 Months



5-Year Treasury Note Yield - Last 12 Months



2-Year Treasury Note Yield - Last 5 Years



5-Year Treasury Note Yield - Last 5 Years

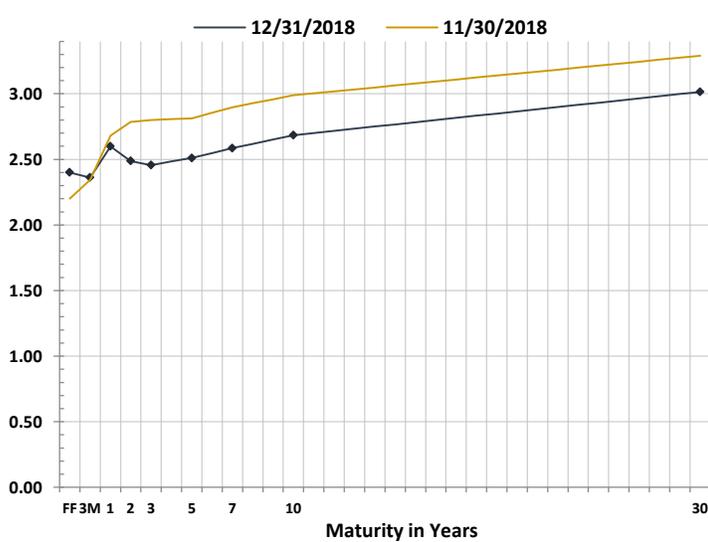


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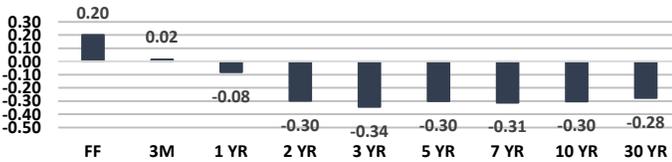
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Treasury Month-Over-Month



Month-Over-Month Change in Treasury Yields



Global Stock Performance

	Value	MTD Change	QTD Change	YTD Change
Dow Jones	23,327	-8.66% ↓	-11.83% ↓	-5.63% ↓
S&P 500	2,507	-9.18% ↓	-13.97% ↓	-6.24% ↓
Nasdaq	6,635	-9.48% ↓	-17.54% ↓	-3.88% ↓
Stoxx Europe 600	338	-5.55% ↓	-11.88% ↓	-13.24% ↓
China CSI 300	3,011	-5.11% ↓	-12.45% ↓	-25.31% ↓
Nikkei 225	20,015	-10.45% ↓	-17.02% ↓	-12.08% ↓

Global Sovereign Debt Performance

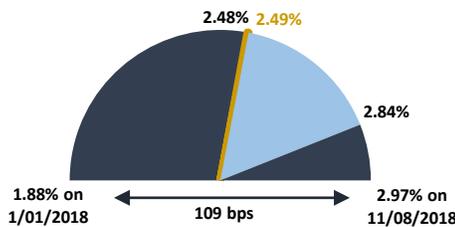
	Yield	MTD Change (in bps)	QTD Change (in bps)	YTD Change (in bps)
U.S. 2-year	2.49%	-29.9 ↓	-33.1 ↓	60.5 ↑
U.S. 5-year	2.51%	-30.1 ↓	-44.2 ↓	30.5 ↑
U.S. 10-year	2.68%	-30.4 ↓	-37.7 ↓	27.9 ↑
German 10-year	0.24%	-7.1 ↓	-22.8 ↓	-18.5 ↓
U.K. 10-year	1.28%	-8.7 ↓	-29.6 ↓	8.7 ↑
French 10-year	0.71%	2.6 ↑	-9.4 ↓	-7.5 ↓
Italian 10-year	2.74%	-47.1 ↓	-40.5 ↓	72.6 ↑
Japanese 10-year	0.00%	-8.9 ↓	-12.7 ↓	-4.5 ↓

Commodity Performance

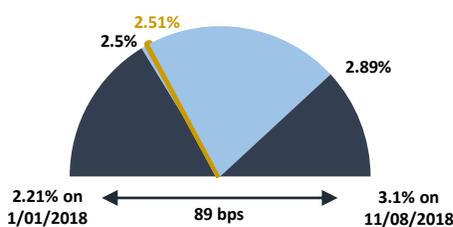
	Value	MTD Change	QTD Change	YTD Change
WTI Crude	\$ 45.41	-10.84% ↓	-38.01% ↓	-24.84% ↓
U.S. Dollar	96.17	-1.13% ↓	1.09% ↑	4.40% ↑
Gold Spot	1,282	4.90% ↑	7.54% ↑	-1.58% ↓
Commodity Index	76.72	-7.08% ↓	-9.96% ↓	-12.99% ↓

Treasury Notes Intraday Ranges: 52-Week Yield Range / Monthly Yield Range / Last Traded Yield

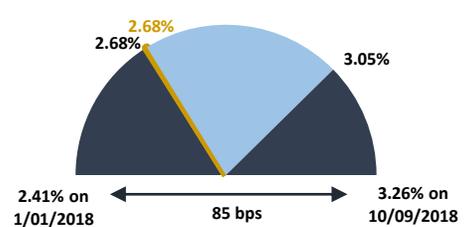
2-Year Treasury



5-Year Treasury



10-Year Treasury



Nonfarm Payrolls

November 155k

Unemployment Rate

November 3.7%  
Unchanged

Existing Home Sales MoM

November 1.9%

New Home Sales MoM

Existing home sales rose for the second time in eight months (3rd weakest since 2016); New home sales data postponed by government shutdown

Core Retail Sales

November 0.9%

Consumer Confidence

December 128.1  
Down 8.3 pts  
Five-month low

ISM Non-Manufacturing

November 60.7  
+0.4 pts  
Non-manufacturing 2nd best since 2005

ISM Manufacturing

November 59.3  
+1.6 pts

Manufacturing Production

November 0.0%

Core Capital Goods Orders

November -0.6%  
Weaker-than-expected despite positive October revisions

Trade Balance

October -55.5B  
-0.9B  
Widest since 2008

Core PCE YoY

November 1.9%  
Up 0.06%

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