



March Market Update: Trade-War Roils Markets as Fed Signals for Steeper Rate-Hike Path

March was a dramatic month for global equities, as an escalating trade war between China and the United States put investors on high alert. On the monetary policy front, the Federal Reserve raised interest rates as expected, but signaled for a steeper rate-hike path in the future.

Trump Escalates Tariff War with China

President Donald Trump pushed his protectionist agenda last month, holding true to a spate of campaign promises designed to close the U.S. trade gap with the rest of the world.

On Mar. 8, the president signed an order authorizing tariffs on steel and aluminum imports. The proclamation exempted allies Canada and Mexico, which are part of ongoing efforts to renegotiate the North American Free Trade Agreement (NAFTA). The order imposes a 25% tax on steel and 10% on aluminum.

On Mar. 22, President Trump imposed new tariffs on about \$50 billion worth of Chinese imports, a bold move that has divided the Republican administration. Less than two weeks later, the Office of the U.S. Trade Representative produced a list of over 1,000 goods that will be subject to higher tariffs.¹

It didn't take long for the Chinese to respond. On Apr. 3, Beijing proposed \$50 billion in retaliatory tariffs on U.S. goods, setting the stage for a clash of superpowers.

Washington's trade deficit with China swelled to a record \$372.5 billion in 2017, putting more onus on the Trump administration to fight back.²

Stock Markets Falter

Equity markets from New York to Shanghai finished in the red last month, as trade-war risks dampened investors' appetite for riskier assets. On Wall Street, the major indexes fell between 2.7% and 3.7% during the month, prolonging the months long correction in the market.

Canadian stocks also fell, with the TSX Composite Index shedding 2.2% from its monthly high and 0.4% overall.

Technology stocks were at the center of the selloff, fueled in part by Facebook's Cambridge Analytica scandal. The so-called FAANG stocks (Facebook, Apple, Amazon, Netflix and Google parent Alphabet) plunged \$324 billion between Mar. 12 and April 2.³

As stocks declined, volatility rose, with the CBOE VIX climbing back above its historic average in the latter half of the month. The VIX, which usually trades inversely with the S&P 500 Index, touched a high near 25.00 on Mar. 23.

Fed Adopts More Hawkish Tone

The U.S. Federal Reserve raised interest rates on Mar. 21, as expected, and signaled a steeper path of rate-hikes in the future. The quarter point increase was the sixth upward adjustment in the last three years.⁴

Policymakers maintained their outlook for three rate increases this year but revised their projections for 2019 and 2020 to reflect four upward adjustments each year. This is broadly consistent with the view put forward by Goldman Sachs, although the investment bank says the Fed will hike a total of four times this year.⁵

Solid job growth and the return of inflation are making it easier for officials to normalize monetary policy. However, the U.S. economy faces significant headwinds in the form of geopolitical risks, record debt levels and a downshift in consumer spending.

The Fed's policy-setting board is not scheduled to meet again until May.

The Month Ahead

Corporate earnings will dominate the headlines in April in what is expected to be a solid quarter for Wall Street. Revised forecasts from FactSet, a U.S. financial research firm, show earnings growth of 17.3% for S&P 500 companies during the first quarter. That's the highest since 2011 and a huge improvement over the previous forecast calling for 11.4% growth.⁶

On the monetary policy front, the Bank of Canada will hold its next interest rate meeting on Apr. 12. Officials are expected to remain on the sidelines as NAFTA negotiations conclude.

Economic data will provide investors with the final puzzle pieces in gauging the health of the global economy during the first quarter. Reports on inflation, employment and consumer spending will be top of mind as the month rolls along.

Sincerely,

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¹ Sam Bourgi (Apr. 4, 2018). "Flamethrowers and Semiconductors: Inside Trump's New China Tariffs." Hacked.com

² An Swanson (Feb. 6, 2018). "U.S.-China Trade Deficit Hits Record, Fueling Trade Fight." The New York Times.

³ Akane Otani, Michael Wursthorn and Ben Eisen (Apr. 2, 2018). "Technology Shares Plunge Again Amid Growing Backlash." The Wall Street Journal.

⁴ Karl Russell (Mar. 21, 2018). "Why the Fed Raised Rates for the Sixth Time in Three Years." The New York Times.

⁵ Shelly Hagan (Mar. 26, 2018). "Goldman Says There's No Need to Worry About Slowing Global Growth." Bloomberg Markets.

⁶ FactSet (Mar. 29, 2018). Earnings Insight: Key Metrics.