

## Volatility Spikes Amid Political and Geopolitical Tensions

**August 21, 2017** – U.S. stocks erased intra-day gains on Friday, capping a second straight weekly loss for the S&P 500. Wall Street was beset by a return of volatility, stemming largely from political drama out of Washington D.C. and a series of terrorist attacks in Spain and Finland. All three major domestic equity averages finished the week at their lowest levels since July as investors responded to news the Federal Reserve retained a hawkish rate outlook despite soft inflation, European concerns about a too-strong euro, and denied rumors of a rift between President Trump and his trusted top economic adviser, Gary Cohn, who was reportedly upset over a botched presidential response to the violent conflicting protests in Charlottesville, Virginia. Stocks swung from opening losses to gains and back again after a report Friday that Steve Bannon was ousted from his White House chief strategist job. Overall, investors are growing dismayed that recent controversies, both foreign and domestic, are making it much more difficult for a divided Congress to work with President Trump to pass his pro-growth policy goals.

The VIX Volatility Index spiked by over 32% on Thursday, helping send the Dow Industrials down 1.2% for its first 1% or greater drop in 64 consecutive sessions, while the broader S&P 500 lost 1.5% for its second-worst trading day this year. For the S&P 500, it was the first time since the June 2016 Brexit announcement that the index fell 1% or more and declined the next day. Key economic data was favorable last week, with July retail sales rising the most this year at twice the level projected (0.6% vs. 0.3%), and a weaker U.S. dollar helped support a 0.4% lift on export prices. The New York Fed’s Empire manufacturing activity index surged to its highest level in three years, while housing construction starts slumped 4.8% last month. Lastly, a reading of consumer sentiment from the University of Michigan jumped to seven-month high for August.

For the week, the S&P 500 fell 0.58%, the Dow Industrials declined 0.77% and the NASDAQ Composite lost 0.57%. Within the S&P 500, 6 of its 11 major sector groups ended negative last week, with Energy (-2.44%) and Telecom (-1.83%) down the most. U.S. crude oil prices slipped by 0.63% to \$48.51/barrel as rising domestic oil production offset a notable weekly pullback in stockpiles. Surprisingly, gold futures slipped 0.42% during the week to end at \$1,283.95/oz., while the U.S. Dollar Index rose 0.39% to 93.434. Treasury prices also edged lower, sending the yield on 10-year Treasury notes up less than 1 basis point to 2.195%. Over the past two weeks, the S&P 500 now stands 2.1% below its all-time high of 2,481, set on August 7<sup>th</sup>.

### What We’re Reading

[Best Retail Sales Data in 2017 ↗](#)

[Eurozone GDP Growth Tops Forecasts ↗](#)

[Yellen Headlines Jackson Hole Symposium ↗](#)

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### Week’s Economic Calendar

**Monday, Aug 21:** Chicago Fed National Activity Index;

**Tuesday, Aug 22:** FHFA House Price Index, Richmond Fed Mfg Index;

**Wednesday, Aug 23:** Mortgage Applications, New Home Sales;

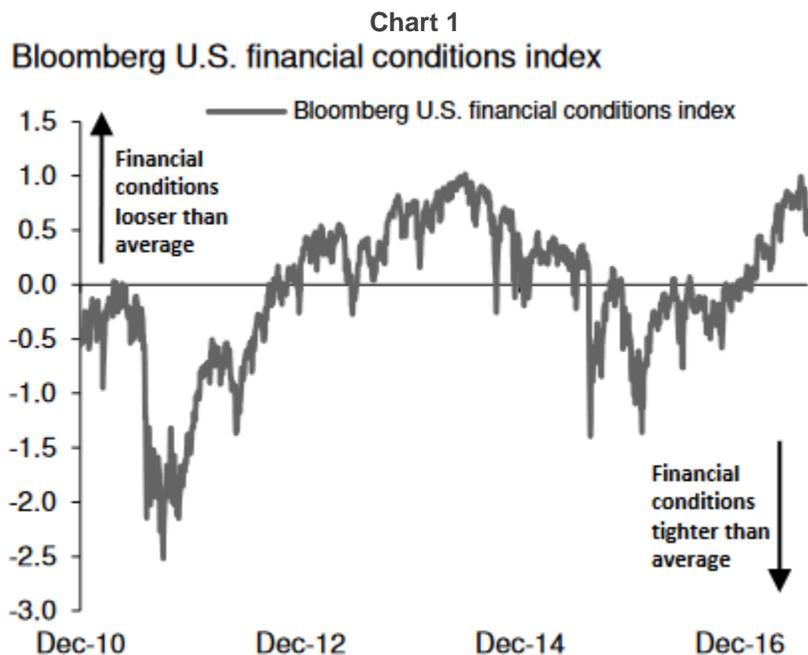
**Thursday, Aug 24:** Jackson Hole Economic Symposium Opens, Jobless Claims, PMI Composite, Existing Home Sales;

**Friday, Aug 25:** Durable Goods Orders.

## Market Watch

Stocks	1-Week	MTD	3-Month	YTD	1-Year	3-Year
Dow Jones Industrial Avg.	-0.84%	-0.99%	4.90%	9.67%	16.56%	8.78%
S&P 500	-0.58%	-1.64%	3.05%	9.76%	13.24%	9.44%
NASDAQ Composite	-0.58%	-1.94%	2.95%	16.33%	20.02%	12.64%
Russell 3000	-0.62%	-1.95%	2.72%	8.82%	12.98%	8.90%
MSCI EAFE	0.07%	-0.82%	3.14%	16.13%	15.26%	2.79%
MSCI Emerging Markets	1.63%	-0.52%	8.38%	24.84%	18.24%	1.81%
<b>Bonds</b>						
Barclays Agg Bond	0.07%	0.48%	1.11%	3.21%	0.06%	2.62%
Barclays Municipal	0.00%	0.47%	1.60%	4.90%	0.61%	3.44%
Barclays US Corp High Yield	0.02%	-0.69%	1.16%	5.36%	8.29%	4.68%
<b>Commodities</b>						
Bloomberg Commodity	-0.54%	-1.32%	0.03%	-4.40%	-3.41%	-12.44%
S&P GSCI Crude Oil	-0.63%	-3.01%	-2.01%	-9.42%	-0.47%	-19.63%
S&P GSCI Gold	-0.19%	1.43%	2.83%	12.15%	-4.84%	-0.20%

## Chart of the Week: U.S. Financial Conditions Have Been Accomodative



Source: Bloomberg, J.P. Morgan Asset Management.

Following last week's spike in equity market volatility due to rising geopolitical tension, markets have begun to sink back into their summer lull as investors refocus on fundamentals. Strong earnings, low interest rates and solid economic data have led to easier financial conditions, which, along with low realized and macroeconomic volatility, has pushed implied volatility, as measured by the VIX, to very low levels. As shown in this week's chart, financial conditions have been more

accommodative than average since the start of 2017, with low interest rates holding both company and household interest costs low, and meaningful earnings growth putting more money in the pockets of both investors and corporations. Supportive financial conditions have also coincided with solid economic performance – as evidenced by strength in retail sales, business optimism and further tightening in the labor market – supporting J.P. Morgan Asset Management’s view that U.S. economic growth should continue at a slow-but-steady pace. While investors may remain concerned with the low volatility environment, history tells them that markets have historically been able to push higher following periods of low volatility, particularly when the fundamentals look solid. As such, continued economic momentum and strong earnings growth should provide support for the U.S. equity market despite a backdrop of elevated valuations and political uncertainty.

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## Glossary

The **Barclays U.S. Treasury: U.S. TIPS Index** includes all publicly issued, U.S. Treasury inflation-protected securities that have at least one year remaining to maturity, are rated investment grade, and have \$250 million or more of outstanding face value.

The **Bloomberg Barclays US Aggregate Bond Index**, which was originally called the Lehman Aggregate Bond Index, is a broad based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate debt securities, MBS (agency fixed-rate and hybrid ARM pass-throughs), ABS and CMBS (agency and non-agency) debt securities that are rated at least Baa3 by Moody's and BBB- by S&P. Taxable municipals, including Build America bonds and a small amount of foreign bonds traded in U.S. markets are also included. Eligible bonds must have at least one year until final maturity, but in practice the index holdings has a fluctuating average life of around 8.25 years. This total return index, created in 1986 with history backfilled to January 1, 1976, is unhedged and rebalances monthly

The **Bloomberg Barclays U.S. Corporate (Investment Grade) Bond Index** measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD-denominated securities publicly issued by U.S. and non-US private-sector industrial, utility and financial issuers. Certificates of deposit are also included. Launched in July 1973, securities included must be rated investment grade (Baa3/BBB-/BBB- or higher). Eligible senior and subordinated corporate securities must have at least one year until final maturity, but in practice the index holdings has a fluctuating average life of around 10.75 years. The index is unhedged and rebalances monthly.

The **Bloomberg Barclays US Corporate High Yield Index** measures the USD-denominated, non-investment grade, fixed-rate, taxable corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch, and S&P is Ba1/BB+/BB+ or below, excluding emerging market debt. Payment-in-kind and bonds with predetermined step-up coupon provisions are also included. Eligible securities must have at least one year until final maturity, but in practice the index holdings has a fluctuating average life of around 6.3 years. This total return unhedged index was created in 1986, with history backfilled to July 1, 1983 and rebalances monthly.

The **Bloomberg Barclays US Municipal Bond Index** covers the USD-denominated long-term tax exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds, and pre-refunded bonds. Many of the subindices of the Municipal Index have historical data to January 1980. In addition, several subindices based on maturity and revenue source have been created, some with inception dates after January 1980, but no later than July 1, 1993. Eligible securities must be rated investment grade (Baa3/BBB- or higher) by Moody's and S&P and have at least one year until final maturity, but in practice the index holdings has a fluctuating average life of around 12.8 years. This total return index is unhedged and rebalances monthly

The **Bloomberg U.S. Treasury Floating Rate Bond Index** is a rules-based, market value-weighted index engineered to measure the performance of floating rate U.S. Treasury bonds. The index inception date is January 31, 2014—the first month-end following the U.S. Treasury's issuance of a floating rate bond. Historical performance and characteristics are available from January 31, 2014, when floating rate notes were offered and first traded, the first new Treasury security since the introduction of Treasury-Inflation-Protected Securities (TIPS) in 1997.

The **Bloomberg Barclays US Convertible Bond > \$500MM Index** is designed to represent the market of US convertible securities, such as convertible bonds, with outstanding issue sizes greater than \$500 million.

The **Bloomberg Commodity Index** is a broadly diversified index that measures 22 exchange-traded futures on physical commodities in five groups (energy, agriculture, industrial metals, precious metals, and livestock), which are weighted to account for economic significance and market liquidity. No single commodity can comprise less than 2% or more than 15% of the index;

and no group can represent more than 33% of the index. However, between rebalancings, group weightings may fluctuate to levels outside the limits. The index rebalances annually, weighted 2/3 by trading volume and 1/3 by world production.

The **CBOE Volatility Index® (VIX®)** is a key measure of market expectations of near-term volatility conveyed by S&P 500 stock index option prices. Introduced in 1993, the VIX Index has been considered by many to be the world's premier barometer of investor sentiment and market volatility.

The **Dow Jones Industrial Average** is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the NASDAQ.

The **MSCI ACWI Index** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets. The MSCI ACWI consists of 46 country indexes comprising 23 developed and 23 emerging market country indexes. The developed country indexes include: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, the United Kingdom and the United States. The emerging market country indexes included are: Brazil, Chile, China, Colombia, Czech Republic, Egypt, Greece, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Peru, Philippines, Poland, Qatar, Russia, South Africa, Taiwan, Thailand, Turkey and United Arab Emirates.

The **MSCI EAFE Index** is designed to measure the equity market performance of developed markets (Europe, Australasia, Far East) excluding the U.S. and Canada. The Index is market-capitalization weighted.

The **MSCI Emerging Markets Index** is designed to measure equity market performance in global emerging markets. It is a float-adjusted market capitalization index.

The **NASDAQ Composite Index** includes all domestic and international based common type stocks listed on The NASDAQ Stock Market. The NASDAQ Composite Index is a broad based index

The **NASDAQ-100 Index** includes 100 of the largest domestic and international non-financial companies listed on The NASDAQ Stock Market based on market capitalization.

The **Russell 2000 Index** measures the performance of the small-cap segment of the U.S. equity universe and is a subset of the Russell 3000 Index representing approximately 10% of the total market capitalization of that index. It includes approximately 2000 of the smallest securities based on a combination of their market cap and current index membership.

The **Russell 3000 Index** measures the performance of the largest 3,000 U.S. companies representing approximately 98% of the investable U.S. equity market.

The **Russell Midcap Index** measures the performance of the mid-cap segment of the U.S. equity universe and is a subset of the Russell 1000 Index. It includes approximately 800 of the smallest securities based on a combination of their market cap and current index membership. The Russell Midcap represents approximately 31% of the total market capitalization of the Russell 1000 companies.

The **S&P 500** is an index of 500 stocks chosen for market size, liquidity and industry grouping (among other factors) designed to be a leading indicator of U.S. equities and is meant to reflect the risk/return characteristics of the large cap universe.

**West Texas Intermediate (WTI)** is a crude oil stream produced in Texas and southern Oklahoma which serves as a reference or "marker" for pricing a number of other crude streams. WTI is the underlying commodity of the New York Mercantile Exchange's oil futures contracts

The **U.S. Dollar Index** is a weighted geometric mean that provides a value measure of the United States dollar relative to a basket of major foreign currencies. The index, often carrying a USDY or DXY moniker, started in March 1973, beginning with a value of the U.S. Dollar Index at 100.000. It has since reached a February 1985 high of 164.720, and has been as low as 70.698 in March 2008

