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# JOBS AND TRADE IN PERSPECTIVE

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## KEY TAKEAWAYS

Headlines related to trade and the March jobs report led to market weakness last week.

While the risk of further escalation of trade disagreements exists, the United States and China remain open to negotiations.

The March jobs report missed expectations, but the labor market overall remains on solid footing.

**Increasing trade tensions weighed on markets during the first week of April, and a weak March jobs report added to concerns, but in this market a little perspective can go a long way.** The S&P 500 Index fell on April 6, but the drop may have seemed worse for investors because January 2017–January 2018 was one of the least volatile periods for the index in history. The S&P 500's 2.2% drop ranked as the fifth largest single-day decline year to date. However, compared to 2017, which saw a maximum daily decline of 1.8% in May, and only experienced four days the entire year where stocks dropped more than 1.0%, the move seemed much larger. While a 2.0% or larger move in the S&P 500 may not be the new normal, we believe that we may continue to see increased volatility in 2018 as markets weigh policy decisions and economic data in the short run. However, when we take a step back from the day-to-day fluctuations of individual economic data points and markets, the economy remains on a positive footing. This solid underpinning, combined with continued potential for strong earnings growth (see our [Weekly Market Commentary](#) for a first quarter earnings preview), and the potential impact of fiscal stimulus, leads us to believe markets may have room to move higher in 2018.

## TRADE RHETORIC STRIKES AGAIN

The announcement of further escalation of trade tensions with China served as one of the main reasons behind the April 6 market drop. Trade was a major theme during the 2016 presidential election, and as 2018 began, President Trump started to roll out limited tariffs, beginning small with washing machines and solar panels in late January. On March 1, tariffs of 25% and 10% were announced on steel and aluminum imports, respectively. Affected countries were given an opportunity to make a case for an exception, several of which were granted before tariffs officially went into effect on March 23.

But the real escalation in trade rhetoric started shortly thereafter. On March 22, \$50 billion in tariffs on Chinese imports were announced by the Trump administration in response to China's intellectual property practices. China retaliated first with tariffs on \$3 billion of exports in reaction to the steel and aluminum tariffs, and then with an additional \$50 billion of their own tariffs on U.S. goods in response to the most recent tariffs. The Trump administration responded by announcing the possibility of another \$100 billion in tariffs on Chinese imports. This number is notable on its own given its size, but it is

also important because the total Chinese imports potentially affected by tariffs (approximately \$153 billion), would be more than the total of U.S. goods imported from China, limiting Beijing's ability to retaliate in kind [Figure 1].

While China may not be able to match the United States in tariffs given the trade imbalance, they do have other ways of responding. Chinese leaders indicated that they would defend their interests "at any cost," and had previously floated the possibility of reducing Treasury purchases as one example of a potential countermeasure, though this would have the potential to create problems for China as well. Over the weekend, stories started to leak indicating that at this point China is considering a devaluation of their currency, which would have a number of effects, including making U.S. exports more expensive for Chinese consumers.

An all-out trade war would be disruptive for both the U.S. and Chinese economies, and the ongoing public dialogue means that we could continue to

see market volatility in the near term. However, it is important to note that at this point, most of the tough talk on trade from both sides is just that—talk. Both China and the United States have indicated an openness to dialogue and we remain hopeful that constructive back-channel talks between the leaders of the world's two largest economies may lead to a less dramatic outcome.

## JOBS REPORT DISAPPOINTS, BUT LABOR MARKET REMAINS SOLID

The March employment report was another catalyst for Friday's market weakness, as the month produced 103,000 new jobs, versus a consensus expectation of 185,000. Though February's strong report was revised higher by 13,000 jobs (to 326,000), a negative revision to January led to a total two-month negative revision of -50,000. However, some slowing was expected after February's unusually strong number, and we believe the slowdown is still largely attributable to temporary factors, which can be difficult to gauge from month to month. For example, construction employment was weak in March, but this may have been due to unseasonably cold weather.

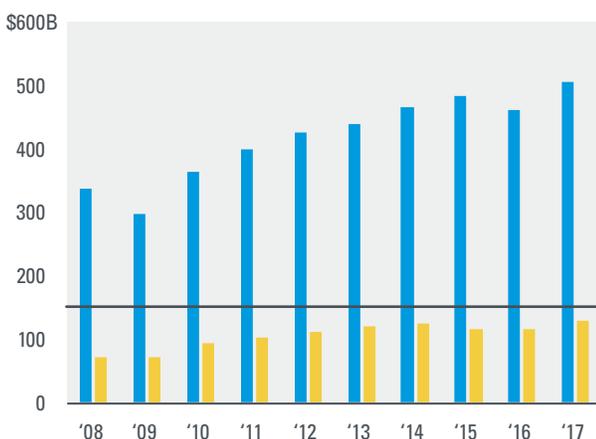
But taking a step back, the two-month average of over 200,000 new jobs per month remains strong for this point in the economic cycle and leaves the overall trend of solid payrolls growth intact. Both the unemployment rate (4.1%) and the underemployment rate (8.0%) are at cycle lows [Figure 2], further reinforcing the idea that the labor market remains in good shape.

## CONCLUSION

Trade rhetoric and the March jobs report caused some market weakness during the first week of April. A true trade war would be problematic

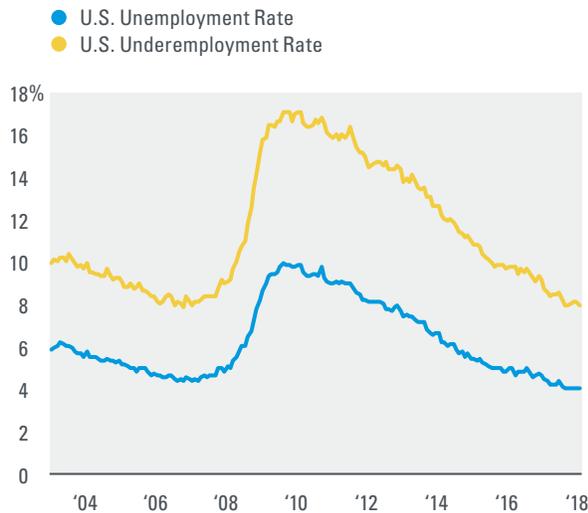
### 1 LATEST TARIFFS MAY EXCEED CHINA'S ABILITY TO RETALIATE IN KIND

- U.S. Imports from China
- U.S. Exports to China
- Current Potential Imports Targeted for Tariffs



Source: LPL Research, U.S. Census Bureau 04/09/18

## 2 UNEMPLOYMENT AND UNDEREMPLOYMENT RATES ARE AT CYCLE LOWS



Source: LPL Research, U.S. Bureau of Labor Statistics 04/09/18

The unemployment rate is the percentage of the total labor force that is unemployed but actively seeking employment and willing to work.

Labor that falls under the underemployment classification includes those workers that are highly skilled but working in low-paying jobs, workers that are highly skilled but work in low-skill jobs, and part-time workers that would prefer to be full time.

for both the U.S. and Chinese economies, and continued discussion on the topic could lead to additional volatility in the near term. However, the fact that both the United States and China seem to be open to dialogue indicates to us that the recent headline-grabbing pronouncements are potentially meant to be negotiating positions rather than final policy. And while the March jobs report missed expectations, the labor market remains strong. Volatility has been higher in 2018 than investors had grown accustomed to; however, we continue to believe that solid economic fundamentals, the possibility of continued earnings strength, and fiscal policy should be positives for markets as the year progresses. ■

### IMPORTANT DISCLOSURES

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### INDEX DESCRIPTIONS

The S&P 500 Index is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

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