

# THE SMITHFIELD Forecast

*A Quarterly Survey of Trends • Seventy Fifth Edition • February 2019*

*For Customers & Friends of*  
SMITHFIELD TRUST COMPANY

## **A NOTE FROM THE CHAIRMAN**

We welcome Kristina Monaco to the Smithfield team. Joining us with prior experience in financial management, Kristina will be an Administrative Assistant with us with a multitude of duties and responsibilities. She has a strong academic background, resting on degrees from Community College of Allegheny County, California University of Pennsylvania and culminating with an MBA from the University of Pittsburgh Katz School of Business.

Kristina and her husband, Michael, and their daughter, Elisabeth, have an American Bulldog and three cats. Kristina shares with me a love of animals and Penguins hockey.

I am confident that all of you who will have interactions with Kristina will find her to be poised, professional and easy to deal with.

— Bob Kopf

## **BRIDLED OPTIMISM**

What a difference a year makes. One year ago, optimism was booming. The US economy was set to explode with the passage of an unexpectedly low 21% corporate tax rate -- plus repatriation, plus spending increases. Macron was at his peak, filling the international void whenever Trump stepped back, ready to pair with Merkel in a new French-German led Euro Area reset. UK Prime Minister May was promoting the pro-UK consequences of Brexit. And Xi Jinping had just been appointed President for life. Recently, pessimism has ruled, with equity markets down around the world, a trade war simmering, weak domestic economies feeding nationalism, and world leaders on the back foot. Yet, after bottoming on Christmas Eve, the equity markets have rallied as Federal Reserve Chair Powell became more dovish, trade negotiations are progressing, and China is pouring fresh fuel on their guttering economic fire. Bottom line, the twin policies of higher interest rates and punitive tariffs, which blunted the impact of tax cuts and spending hikes – and slowed global growth -- are now being reconsidered. We feel the outlook is now looking up for the rest of 2019 and beyond.

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Last year, we argued that the late cycle tax cut and spending hikes would fuel booming growth, but that it would be a sugar high as rising interest rates, wages and energy prices narrowed margins. We suggested a significant equity market correction and an economic slowdown in 2019. Now that equities have bounced off bear market levels, we still expect a retest in early 2019 -- and expect the damage done by weaker asset values will cool -- but not recess -- the US economy near midyear. However, globally, weakness in 2018 means the policy mix should shift back toward stimulus in 2019. This bodes well for equities by year end and the real economy in 2020 -- if policymakers don't regress. Our core view is that near term investor caution will lead to stimulus and fresh optimism by year end. The most optimistic sign for the global economy in 2019 is that the Chinese are not waiting. We feel the major global policy change this year is not the likely stall in US tightening, or a cooling of the earlier US fiscal impetus, or Brexit, or the start of European monetary tightening -- all of which are coming. It is the massive stimulus underway in China, which we now estimate at about 4.5% of GDP. To put that in perspective, the US used fiscal stimulus of about 5.5% of GDP to jumpstart the economy in 2009 after the Great Financial Crisis. If the amount of stimulus implies a far weaker China in 2018 than expected, their slump alone may be as much as a 1% drag on global growth.

We focus on China because their manufacturing intensity makes them the leader in global economic cycles -- down in 2018 and back up, we expect, in 2019. This role was once played by the US Sunbelt. Before globalization, recessions were felt first in Atlanta and Phoenix, because they grew as industrial jobs shifted South and West. Critically, they accounted for the bulk of housing, the most interest rate sensitive sector, which led downturns caused by monetary contraction. However, the advantage of the Sunbelt was its lower cost (labor, regulatory and taxes), so as it cooled, creating fresh slack, firms operating elsewhere

-- often with squeezed margins at the top of their regional cycle -- moved. The Sunbelt also exported part of its recession to the commodities producers who supplied them, via lower prices as manufacturing demand waned. Ultimately, the key to any recovery is lower operating costs, making it more profitable for businesses to supply their customers. Add in easier credit, allowing a faster rebound in demand -- led by housing in the Sunbelt -- and away you go.

As we look around the world today, that is exactly what we see. China has led each of the last two global cycles -- 2015 and 2018 -- caused by credit crunches started in their own domestic market. The 2015 episode is far easier to see as a global slowdown, because domestic policy was relatively quiet in Europe and the US. A faltering China caused a drop in global investment that pushed global equities sideways to down in 2015. A commodity led drop in inflation stalled the Federal Reserve's rate increases. European and Japanese manufacturing suffered from a loss of exports and investments, first to Asia and consequently the world -- and later more of their firms moved to expand in Asia.

The current cycle looks similar with a new Chinese credit crunch starting early in 2018. However, the Trump tax cuts and fiscal stimulus softened the blow for China -- and their trade gap swelled. It was the trade war starting midyear that exposed China's domestic weakness. As a result, global financial markets have slumped, likely near mid-correction now. Meanwhile, European industrial production data are bordering on recession for the second half of 2018 -- just as the European Central Bank, still looking at a regional economic model, wants to begin tightening! Bottom line, with multinationals hunting the world for the best investment opportunities, we no longer have US, or European, or Asian economies. We live in one global economy where a policy mistakes in any large bloc -- NAFTA, the Euro Area, or China (plus its commodity producing vassals in the emerging markets) -- affects all.

The US stock market just marked the need for a Fed pause and a trade truce – but it will be months before the economy sees those policies take hold. Guideposts for the all clear include the Fed skipping the March tightening, a modest rise in the unemployment rate to ease very tight labor markets, any bipartisanship vis a vis the economy from Washington, and any agreement to begrudgingly get along with China – until both economies start to recover. But if China rebounds more and sooner than the US, Sino-US head butting will likely reappear before the 2020 election and China’s Party centennial.

In any case, we see a flat recovery ahead for the real economy, as in 2001-2003 and 2010-2016. While heavy investment in China was the driver of the global economy since the Chinese entered WTO in 2000, that will be far more difficult ahead. Any factory floor replacement – whether in the ASEAN, India, Mexico, or Eastern Europe – will be far smaller and less homogenous, so multinational corporate risk takers will be more cautious. After all, no one walks into a dark room fast – especially barefoot.

Cycles wax and wane, and it looks to us as if this one is bouncing along its bottom. That process usually does not take more than a year (as was true even after the Great Financial Crisis in 2008). As a result, we are shifting to a more optimistic tone for 2019 – and into 2020. As always, a fresh policy mistake, especially in the US, could lengthen the corrective period, but we are currently quite confident we will soon see a Sino-US trade truce, that USMCA is signed into law, that the Federal Reserve’s next move may be to ease (later in 2019), and that summer – rather than winter – is now coming.

— Michael Drury

## SMITHFIELD TRUST COMPANY BOOK REVIEWS

### THE SOUL OF AMERICA: THE BATTLE FOR OUR BETTER ANGELS

By: *Jon Meacham*

Lincoln’s words in his first Inaugural Address in 1861 are hauntingly current today: “We are not enemies, but friends. We must not be enemies. Though passion may have strained it must not break our bonds of affection. The mystic chords of memory...will yet swell the chorus of the Union when again touched, as surely they will be, by the **better angels of our nature.**”

Meacham sets out to calm our fears of today’s calamitous times by stating in his introduction, “For many, the fact that we have arrived at a place in the life of the nation where a grand wizard of the KKK can claim, all too plausibly, that he is at one with the will of the president of the United States seems an unprecedented moment. History, however, shows us that we are frequently vulnerable to fear, bitterness, and strife. The good news is that we have come through such darkness before.”

He makes his case for hope overcoming fear numerous times in our nation's history by examining seven historical times where, at least to some of us, things seemed pretty bleak. Whether it was right after the Civil War when the KKK ruled throughout the South and the Lost Cause was gaining momentum, TR's progressivism cloaked as it was in white supremacy, the struggle of women for the right to vote during the Wilson Administration, FDR's efforts to deal with terrible economic times while not addressing the plights of blacks in this country and Jews abroad, the McCarthy era, and LBJ's quest for civil rights for blacks, Meacham pulls no punches. And, he tells the stories well.

I highly recommend this book, especially for those of us who are worried about the fate of our Republic. Meacham gives me pause. Maybe, just maybe, we have been here before. But, I'd like a discussion with him...

— Tim Merrill

## THE CODDLING OF THE AMERICAN MIND

By: *Greg Lukianoff and Jonathan Haidt*

There are disturbing trends on many college campuses today. Controversial speakers are shouted down, free speech is increasingly restricted, and students are demanding "safe spaces" on campus. Lukianoff and Haidt date these trends to 2013, the year that "I-gen," the generation following the millennials, first arrived on campus.

The authors note that young people suffer increasingly from anxiety and depression, and there are increased incidents of suicide among today's teenagers. They attribute this to several cultural changes in our society, including the overuse of social media, the rise of "helicopter parenting," and the extreme political polarization in the country. Underlying much of this are three great untruths which have come to be accepted by young people:

- What doesn't kill you will make you weaker.
- Always trust your feelings.
- Life is a battle between good people and evil people.

For anyone concerned about today's youth or the state of college campuses, this book is a wealth of information. Lukianoff is the president of F.I.R.E. (Foundation for Individual Rights in Education), and so is well versed on today's campus culture. Haidt is a PhD psychologist who has several previous books including "The Righteous Mind," in which he explores why people of differing political viewpoints cannot communicate with each other.

— Henry Haller, III

## 4 3 2 1

By: *Paul Auster*

A good friend suggested that I expand my horizons with a somewhat rare foray into fiction. The foray proved to be a painful experience.

“4 3 2 1” is a bildungsroman. (I must confess that this word sent me on a run to my trusted Noah Webster dictionary.) A bildungsroman is a novel which details the maturation, psychological development and moral education of a principal character. In this case the principal character is Archie Ferguson, a Jewish kid born in New York City in 1947 with an improbable Christian name. The author of “4321” writes with a “stream of consciousness” style, which captures well the musing of Archie especially before age 12, but has the disadvantage of making a long book even longer.

The added twist in this novel is that the author presents the reader with four stages of Archie’s maturation on parallel tracks, telling them chronologically and essentially simultaneously. In what is presumably an autobiographical explanation of this fictional technique, Paul Auster describes Archie Ferguson’s creation of his own novel as follows:

“Identical but different, meaning four boys with the same parents, the same bodies, and the same genetic material, but each one living in a different house in a different town with his own set of circumstances. Spun this way and that by the effect of those circumstances, the boys would begin to diverge as the book moved forward, crawling or walking or galloping their way through childhood, adolescence, and early manhood as more and more distinct characters, each one on his own separate path, and yet all of them still the same person, three imaginary versions of himself, and then himself thrown in as Number Four for good measure, the author of the book, but the details of the book were still unknown to him at this point, he would understand what he was trying to do only after he started doing it, but the essential thing was to love those boys as if they were real, to love them as much as he loved himself... . Only one thing was certain. One by one, the imaginary Fergusons would die...but only after he had learned to love them as if they were real, only after the thought of seeing them die had become unbearable to him, and then he would be alone with himself again, the last man standing. Hence the title of the book: 4 3 2 1.”

“4 3 2 1” has two paramount themes: sex and death. Many of the sexual themes in the book are, at least for me, too graphic, sordid, disgusting and revolting. The obsession with death is truly depressing. As the novel marches along with these two themes, it becomes increasingly tedious.

While “4 3 2 1” has received rave reviews from most critics, I am happy to be a contrarian here and say that unless you are (to use a slang term from my children) a weirdo, go elsewhere for your literary pursuits.

— Bob Kopf

## THE HOPKINS TOUCH

By: *David L. Roll*

Undoubtedly President Franklin Roosevelt's most influential, powerful and trusted advisor, Harry Hopkins was arguably the glue which kept the fragile alliance between Roosevelt, Winston Churchill and Joseph Stalin together in a valiant effort to defeat Hitler in World War Two. The author describes in a deft and readable manner how Hopkins had the unique ability to ingratiate himself to powerful people without forfeiting his effectiveness in moving them to more reasonable and accommodating positions.

I have previously learned from my friend Paul Reid's Churchill biography, "The Last Lion," about the importance of Hopkins in bringing Churchill and Roosevelt together. In reading David Roll's account of Roosevelt's near abandonment of Churchill in favor of Stalin near the end of the war, I now have a greater appreciation of Roosevelt's reasons to appease Stalin. According to the author, both Roosevelt and Hopkins were terrified that Stalin would, once again, enter into a peace treaty with Hitler, thus allowing the Germans to turn the full force of their war capabilities against the Allies in Western Europe. Reasonable people can have a rational debate as to whether the Roosevelt/Hopkins placating of Stalin went too far.

Roll's investigation of Hopkins' personal side is also good reading. His relationship with his second wife, Louise, has its bizarre aspects, including Harry's possible request to have J. Edgar Hoover of the FBI wiretap Louise.

I urge all my dear readers to consider this splendid biography.

— Bob Kopf

## JOHN MARSHALL

By: *Richard Brookhiser*

Richard Brookhiser is one of my favorite biographers. He writes incisively, using spare, crisp and understandable prose. His new biography of Chief Justice John Marshall, our country's most eminent jurist, is no exception.

Idolizing George Washington (with whom he served in the Revolutionary War) as the greatest man he ever encountered, John Marshall adopted Washington's vision of a unified nation in crafting well-reasoned opinions on the Constitution from the Supreme Court during his thirty-four years on the bench. His battles with his detested cousin, Thomas Jefferson, and then Andrew Jackson are described wonderfully here.

Marshall's most famous and important decision came in Marbury v. Madison, establishing the principle of judicial review and allowing the Supreme Court to strike down laws enacted in contravention of the Constitution. Brookhiser's explanation of Marshall's thought process and logic in deciding Marbury is remarkable.

I recently reviewed Professor Joel Richard Paul's biography of Marshall in these pages. Paul's book is more com-

prehensive that Brookhiser's, and both are excellent. Since Brookhiser's work is more like the "Cliffs Notes" version of Marshall's life, I wish that I had read his first. Suffice it to say here that you will not be disappointed with reading both volumes.

— Bob Kopf

## **MURDER IN THE COURTROOM: A TRUE STORY OF SEXUAL COMPULSION, JUDICIAL MISCONDUCT AND HOMICIDAL RAGE**

*By: John L. Young and Lyle James Slack*

I grew up in Warren, Pennsylvania (though some of my friends assert that I never did grow up). We lived in a small house on the same block as the Warren County Courthouse. Two weeks before my tenth birthday a construction worker by the name of Norman Moon had a seemingly routine alimony hearing in the Courthouse before Judge Allison Wade in 1954. Enraged, Moon stood before Judge Wade, pulled out a Colt handgun and murdered our respected jurist on the bench in an act never committed elsewhere in our country.

I remember the events surrounding the murder quite well, and I recall Judge Wade and his daughter Ann (then age nine) in general terms, since they lived only one block from us.

Norman Moon's ex-wife was Janet Schwab Moon, born and raised in Warren County. Pretty and promiscuous, Janet was hardly an ideal spouse, and the authors' depiction of the marriage of Norman and Janet is depressing. The authors do portray Norman Moon in a sympathetic light, and they attempt to enhance this sympathetic treatment by casting unwarranted aspersions upon Judge Wade. Specifically, they assert, with no real evidence, that Judge Wade may have murdered his wife in 1952 and, with the same lack of evidence, that Judge Wade may have had sex with Janet Moon. Since Judge Wade was a friend of my parents and had a distinguished reputation, these allegations are offensive to me. Combining this with undistinguished and mediocre writing, one wishes that the authors had not resorted to sensationalism in a so far unsuccessful and lame attempt to put together a movie deal. The sad story of Norman Moon should, on its own, be enough to carry the book. Notwithstanding these shortcomings, you should find the book worthy of your attention.

— Bob Kopf

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