September 1, 2019

The Big Picture and Key Takeaway – August 2019

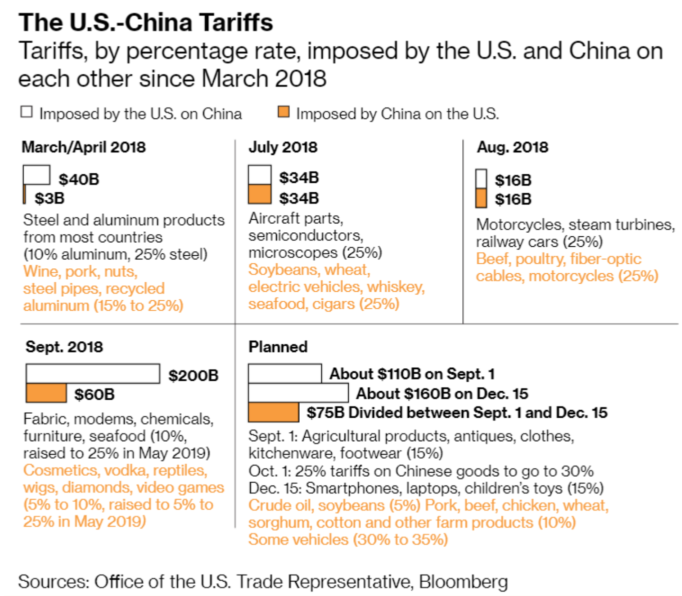
The Big Picture

- The two most significant drivers of the economy and financial markets this year, trade and monetary policy, remain in a serious state of flux. August was whirlwind of He-Said/He-Said on both fronts.

- On monetary policy, Fed Chairman Jerome Powell indicated that that the trade war was without "recent precedent" and the Fed has no "settled rulebook" for international trade issues.

- On trade policy, the U.S. and China volleyed additional tariff threats back and forth towards the end of August, with the actual imposition of some tariffs taking place on September 1st.

- If you're having difficulty keeping track of the trade threats and realities, the chart to the right breaks down all of the *imposed and planned* tariffs levied by both the U.S. and China.



- President Trump expressed his ire via Tweet at both Powell and China, asking simply *"My only question is, who is our bigger enemy, Jay Powell or Chairman Xi?"*

- The upshot is that the trade war does not seem to be blowing over as many had hoped. It also appears to be having an impact overseas as international economic growth has slowed markedly with effects not only felt in Asia, but Europe as well.

- In the U.S., the effect is yet unclear, but that may come into focus soon. According to JP Morgan, the latest round of tariffs on China could cost the average American household up to $1000 a year as product prices rise to offset increased import costs.

- Given all of this, you might think the stock market might price-in the uncertainty via lower prices. While the stock market did drop in August, and was volatile with 11 daily moves of over 1%, it held-in relatively well and remains up over 18%, year to date, in the U.S. (S&P 500). The stock market is taking the more optimistic "wait and see" approach. The bond market, on the other hand, seems to have made its call – with record-low yields and yield curve inversions – slower growth and possibly a recession may be on the horizon. Which market is correct will likely determine whether 2019 is a year of more gain, or impending pain.

The Key Takeaway

Despite all of the drama and volatility, there hasn't been much to complain about this year for diversified investors. Through the end of August, stocks, bonds, and gold are all up rather nicely. Stocks seem to be indicating a rather benign outcome to all of this uncertainty, which would look like a resolution to trade issues and easier monetary policy – a double positive whammy! Bonds are indicating a more negative outlook for the economy – which is good, well, for bonds. It's a nice place to be when everything makes money. But both outcomes cannot ultimately happen. Given where we are in the market and economic cycle, *we would place a little more stock in the outlook being provided by bonds, w*ith a considerable degree of uncertainty surrounding it all.

August & YTD Market Performance

Market Returns		Returns (%)	
Index	Description	August	YTD 2019
S&P 500 TR USD	US - Large Company	-1.58	18.34
Russell 2000 TR USD	US - Small Company	-4.84	11.85
MSCI ACWI Ex USA NR USD	All International, excluding US	-3.09	8.76
MSCI EAFE NR USD	International, excluding Emerging Markets	-2.59	9.66
MSCI Emerging Markets NR USD	Emerging Market Stocks	-4.88	3.90
Bloomberg Barclays US Agg Bond TR USD	High Quality US Bonds	2.59	9.10
ICE BofAML US High Yield TR	Lower Quality US Bonds	0.39	11.15
XAU Gold Spot $/OZ	Gold	7.54	18.54
*Through August 31, 2019 Source: Morningstar, MSCI, Bloomberg			

Global Stocks

Stocks capped off a very volatile month of August with modest losses. Large U.S. stocks fared best on a relative basis, as small U.S. stocks, and international developed and emerging market stocks all performed below the return of the S&P 500 Index. Smaller companies within the U.S. were hurt as they are seen as less economically resilient, at a time where many are questioning the sustainability of the economic expansion in the U.S. and abroad. The U.S. dollar also continued to strengthen relative to a basket of foreign currencies, hurting international stock returns as they are translated back into dollars. But international stocks have also been hurt by a noticeable economic slowing trend overseas, which has become more apparent in bellwether economies like Germany and China. Within the U.S. markets, among individual sectors, defensive sectors such as Utilities and Consumer Defensives produced positive returns. Real Estate also delivered a solid gain in August given declines in interest rates. On the negative side of the ledger, the Energy and Basic Materials sectors were down on falling commodity prices, the economically sensitive Consumer Cyclicals were impacted by slowdown fears and Financial Services by much lower interest rates.

Bonds

Bonds continued to benefit from a decline in interest rates across all maturity levels. The 10-year Treasury bond yield dropped another 0.35% while the 30-Year Treasury Bond finished below 2% for the month, a record low yield level. As rates fall, high-quality bond prices go up, and all major bond market sectors once again produced positive returns for the month and the year. The yield curve once again inverted in August. While the 10-year Treasury yield has been below the 3-month bill yield for a couple of months, it also dropped below that of the 2-year yield for the first time since 2007. The bond market is also signaling meager inflation for a very long time. The difference between the yields on a typical 10-year Treasury Bond and its 10-year Treasury Inflation-Protected Security equivalent, known as the breakeven inflation rate, is now only 1.55%. This means that the bond market is pricing in an annualized inflation rate on of only 1.55% over the next 10-years, which is well below the Federal Reserve's 2% target.

Important Disclosure Information

This report is provided as information and commentary regarding the market. The views expressed in this report are as of the date of the report, and are subject to change based on market and other conditions. This report contains certain statements that may be deemed forward-looking statements. Please note that any such statements are not guarantees of any future performance and actual results or developments may differ materially from those projected.

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Index and Category Definitions

The S&P 500 Index *is a capitalization-weighted index of 500 U.S. stocks.* ***Russell 2000 TR USD*** *is a market cap weighted index* The Russell 2000 measuring the performance of approximately 2,000 smallest-cap American companies ***The MSCI All Country World ex-USA 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 All Country World ex-USA Index consists of 22 developed and 24 emerging market country indices.* ***The MSCI EAFE Index (Europe, Australasia, Far East)*** *is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the U.S. & Canada.* ***The MSCI Emerging Markets (EM) Index*** *is a free float-adjusted market capitalization index that is designed to measure equity market performance of 24 emerging markets countries.* ***Bloomberg Barclays U.S. Aggregate Bond Index*** *is an index of the U.S. investment-grade fixed-rate bond market, including both government and corporate bonds.* ***ICE BofAML U.S. High Yield Index*** *is an unmanaged index of below-investment grade U.S. corporate bonds.* ***XZU Gold Spot $/Oz*** *reflects the exchange rate of* ***Gold*** *against the US dollar* ***index***

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