Early August 2019

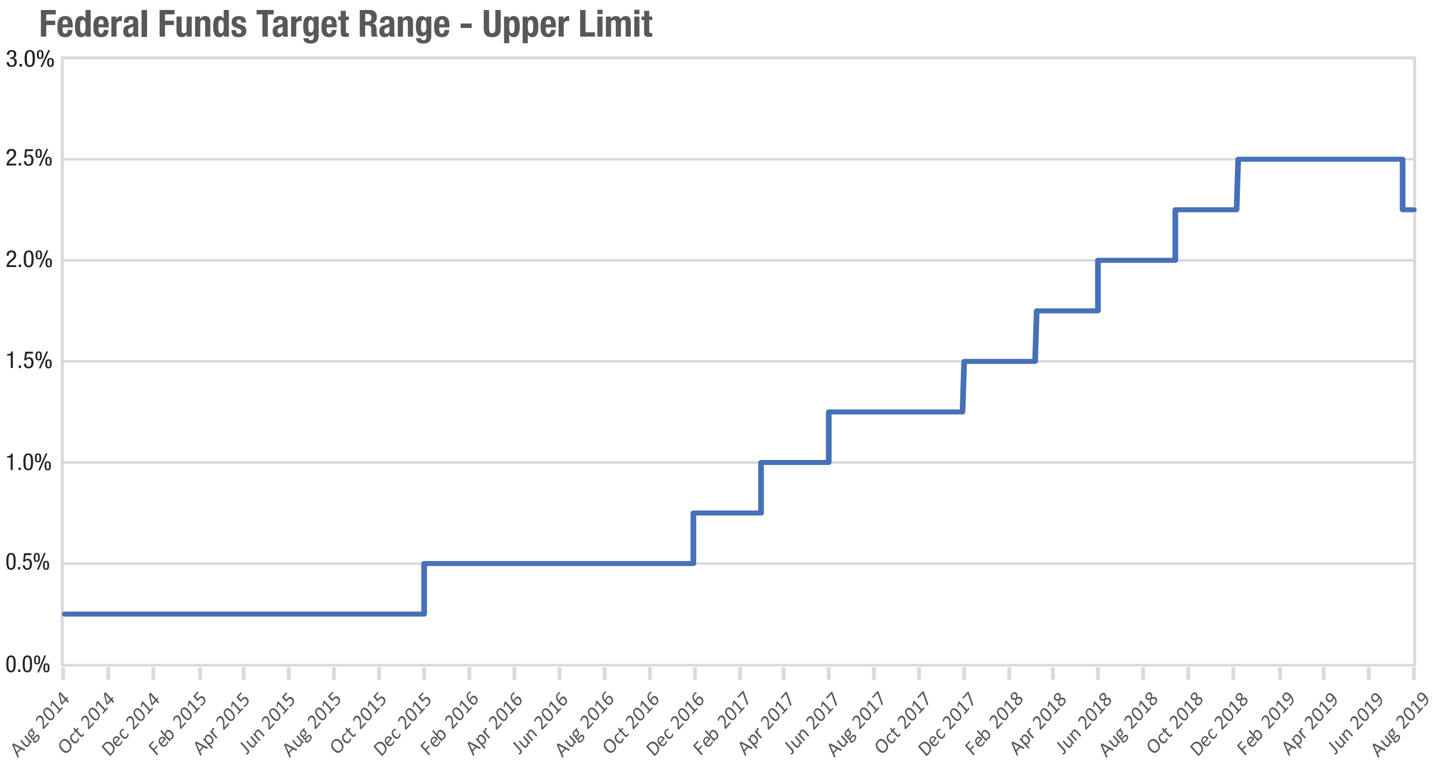
Monthly Market Commentary

Discussion Points

» Record Number of Employed Workers
» Fed Cuts Rates
» Trade War Escalates

The U.S. economy is officially in the longest economic expansion ever, breaking the previous record of 120 consecutive months. The U.S. national unemployment rate remains at 3.7%, and according to the Bureau of Labor Statistics, in July, the U.S. reached a record of 157,280,000 employed individuals. While the U.S. economy is still growing, the rate of growth continues to show signs of slowing. The Leading Economic Index is followed by many investors, as it is a composite of economic data used to predict the outlook for the economy. The index showed no growth from April to May and showed a modest decline in June. This is important because, on average, this index has declined for six to eight months before each of the prior recessions going back to 1962. Despite this, GDP for the second quarter managed to exceed growth expectations of 1.9% as the U.S. economy expanded by 2.1%. Consumer spending increased, which made up for the weakness in businesses investment, housing and U.S. exports. This helped propel gains in the domestic equity markets, as the S&P 500 climbed to a year-to-date return of 20.2%. International markets didn't fare as well, as both the MSCI EM and MSCI EAFE indices pulled back in July, bringing their 2019 returns to 9.2% and 12.6% respectively.

The Federal Reserve remained a primary focus for U.S. investors, as the committee completed their July meeting with a reduction in the overnight lending rate between banks by 0.25%, to a range of 2.0%-2.25%. At the end of July, the Bloomberg Barclay's U.S. Aggregate Bond Index added 0.22%, while the year-to-date return increased to 6.35%. The rate cut was widely anticipated, but it was the first reduction that the Fed made since December 2008. The real surprise was the explanation that Fed Chair Jerome Powell used in explaining the rate cut. He said the committee felt the rate reduction was a "midcycle adjustment." This indicated that it was not the beginning of a series of reductions and that investors should not assume more are likely. Powell went on to say there was "definitely an insurance aspect" to the committee's decision for the rate cut. He also explained that markets would be more capable of absorbing some of the economic shock from fears of slowing global growth and the impact of ongoing trade wars between the U.S. and China.



Source: Federal Reserve Bank of St. Louis

The stock market did not have long to focus on the Fed's rate cut because the very next day President Trump announced a plan to levy a new round of tariffs against China. The new tariffs will be 10% on the remaining $300 billion of China's exports and is slated to commence on September 1, 2019. This announcement reversed the positive momentum that markets were experiencing, as the S&P 500 fell almost 3%, making it the worst performing day of 2019. Oil fell 8% to $53.95 a barrel on fears that China may begin purchasing Iranian crude oil as a defiant act against the economic sanctions that the U.S. has placed on Iran.

In response, China retaliated by halting all future purchases of U.S. agricultural products. The U.S. Census shows that in 2018, China was the fourth largest consumer of U.S. farm exports at $5.9 billion, exceeded only by Mexico, Canada and Japan. At the same time, the Chinese devalued their currency below a psychologically important 7:1 ratio versus the U.S. Dollar for the first time since the 2007-2008 Financial Crisis. With all things being equal, a weaker yuan would make Chinese exports cheaper. In response, the U.S. accused China of being a "currency manipulator" and bond investors flocked to the safety of U.S. Treasuries. Over the next week, bond yields plummeted on the 10-year U.S. Treasury to as low as 1.71%.

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