CLEARBROOK

INVESTMENT COMMITTEE MARKET COMMENTARY

JULY 1, 2019 www.clearbrookglobal.com

U.S. EQUITIES

U.S. equity markets were lower slightly last week as investors focused on the scheduled meeting between President Trump and Xi to discuss trade issues, at the G-20 conference in Osaka, Japan.

a) **Dow Jones -0.45%, MTD +7.31%, YTD +15.40** b) **S&P 500 -0.27%, MTD +7.05%, YTD +18.54%**
c) **Russell 2000 +1.16%, MTD +7.07%, YTD +16.98%**

Drivers: I) **Presidents Trump and Xi announced** on Saturday that **bilateral talks would resume**, and the U.S. would indefinitely suspend the 25% tariffs on the additional $300 billion of Chinese imports which were not presently covered. In addition, Trump said he would permit U.S. firms sell high-tech equipment to Huawei Technologies Co. and China would begin to buy large amounts of American farm products.

II) The **first half of 2019** saw the **major market indexes** touch **new all-time highs**, as the Federal Reserve made a 180 degree turn from a policy of raising interest rates in December, to the decision in March to halt any interest rate rise and delay the run off of the Fed balance sheet. This propelled the S&P 500 higher by 18.54%, led information technology (+27.00%), Technology (+26.98%) and Consumer Discretionary (+21.32%).

III) **Durable Goods** orders **declined 1.3% in May**, but the drop is more modest than the report belies. **Excluding transportation equipment**, specifically a second consecutive decline in civilian aircraft orders and a sharp May drop in orders of **motor vehicles**, **durable goods orders rose 0.3%** to just edge past the Street consensus range. Core capital goods orders (nondefense ex-aircraft) came in on the high end of expectations at a 0.4% gain.

IV) May personal income rose 0.5% to beat expectations by 0.2% while consumer spending rose an expected 0.4% with a 0.3% upward revision to April, now at 0.6%, an unexpected plus. The **core PCE price index rose 0.2%** for a second straight month with the **year-on-year rate steady at 1.6%,** both weak but slightly better than expected. Overall prices also rose 0.2% on the month with this yearly rate down 0.1% to 1.5% which is still 1 tenth better than the Street's consensus.

V) **Equities ended June higher with Small-Cap, Value, Materials and Energy leading equity price performance. The laggards for the month are Large-Cap, Growth and Communication Services.**

Capitalization: **Large Caps +7.02%** (YTD +18.84%), Mid-Caps +6.87% (YTD +21.35%) and **Small Caps +7.07%** (YTD +16.98). **Style: Value** +**8.14%** (YTD +15.93%) and **Growth +7.06%** (YTD +17.37%). **Industry Groups (Leaders):** Information Technology +9.19% (YTD 27.00%), Technology +9.09% (YTD +26.98%), Consumer Discretionary +7.87% (YTD +21.32%), Industrials +7.81% (YTD +21.25%), REITs +1.76% (YTD +20.33%), Consumer Staples +5.27% (YTD +15.93%), Communication Services +1.73% (YTD +15.33%), **Financials +6.71%** (YTD +17.13%), **Materials +11.64%** (YTD +17.08%), Utilities +3.28% (YTD +14.56%), **Energy +9.23%** (YTD +13.02%) and Healthcare +6.61% (YTD +8.00).

EUROPEAN EQUITIES

The MSCI Europe index rose last week by +0.65% on comments from President Trump regarding potential progress in trade talks with China, which offset negative economic data from the European Commission.

Drivers: I) The **German Ifo Survey** showed **business confidence deteriorated** in May, as the indicator dropped 0.5 points versus its unrevised May reading to 97.4. This was a third straight monthly decline for the Survey and its weakest reading since November 2014. The headline fall was attributable to another downgrade to expectations which decreased a full point to 94.2, a four-month bottom, and second worst showing since November 2012.

II) **Eurozone inflation** was **flat** in June, **coming in at 1.2%,** matching both its final May estimate and market expectations. However, more importantly, core prices picked up a little steam. As such, the narrowest gauge which excludes energy, food, alcohol and tobacco, climbed 0.3% to 1.1%, slightly higher than market expectations but still broadly in line with the 2018 average.

III) **Performance of European Indexes for the week, month-to-date and year-to-date. The MSCI Europe Index was higher by +0.65% for the week (MTD +6.72%, YTD +15.80%).**

ASIAN EQUITIES

Asian equity markets rose last week as investors were focused on optimistic signs ahead of the meeting between Presidents Trump and Xi at the G-20 summit. The Dow Jones Asia Index rose by +0.25% for the week, (MTD +4.69%, YTD +5.98%).

Drivers: I) **May retail sales** in **Japan increased 1.2%** on the year, **improving** from the revised growth of **0.4% in April** and matching the consensus forecast. Seasonally adjusted retail sales rose 0.3% on the month after falling 0.1% previously. Stronger year-on-year growth in headline retail sales in May was mostly driven by a rebound in motor vehicle sales, up 2.0% on the year after falling 1.7% previously. Growth in food and beverage sales slowed from 1.5% to 1.2%, with fuel sales also weakening.

II) **Japan's May industrial production** index **rose 2.3%** on the month (seasonally adjusted) after advancing 0.6% in April**, stronger than** the **consensus forecast** for an increase of 0.3%. Stronger headline industrial production reflected increases in the output of motor vehicles, production machinery and electrical machinery. This was partly offset by drop offs in the output of transport machinery and other manufacturing. In year-on-year terms, the index fell 1.8% in May after falling 1.1% previously.

III) **Performance of Asian Indexes for the week, month-to-date and year-to-date. The Nikkei was higher at +0.30% (MTD +3.52%, YTD +7.50%), the Hang Seng Index rose by +0.27% (MTD +6.61%, YTD +10.79%) and the Shanghai Composite declined by -0.77% (MTD +2.77%, YTD +19.45%).**

FIXED INCOME

Treasury yields declined last week as the FOMC opened the door for potential interest rate cuts in 2019, citing the rise in uncertainty caused by the U.S./China trade dispute and continuation of low inflation rates.

Performance: I) **The 10-year Treasury yield was lower last week ending at 2.010% down from 2.059%. The 30-year yield dropped last week, ending at 2.531% down from 2.586%.**

II) **Performance for the week, month-to-date and year-to-date. The Bloomberg Barclays US Aggregate Bond Index rose +0.43% last week, MTD +1.26% and YTD +6.11%. The Bloomberg Barclays US MBS TR advanced by +0.22% last week, MTD +0.72% and YTD +4.17%. The Bloomberg Barclay's US Corporate HY Index was lower by -0.02%, MTD +2.28% and YTD +9.94%.**

COMMODITIES

The DJ Commodity Index was higher by +0.90% last week and is positive month to date +3.12% (YTD +6.92%). Commodities rose last week as agriculture rallied on hopes of progress from the U.S./China trade talks, and oil rallied as OPEC and Russia agreed to continue with their production cuts.

Performance: I) The **price of oil** last week **was higher by +1.04%** up to $58.20 and has risen month to date in June by +9.07% (YTD +28.16%). Oil prices jumped last week as OPEC and Russia agreed to extend their production cuts to March 2020.

II) The **ICE USD Index**, a gauge of the U.S. dollar's movement against six other major currencies, **was higher by +0.04%** at 96.13 for the week (MTD -1.51%, YTD -0.04%). The USD was relatively quiet last week as investors had renewed hope for a potential truce in the US/China tariff wars.

III) **Gold rose last week by +0.67%,** continuing its strongest rally in years as investors continue to expect the U.S. Fed to keep a lid on interest rates. **Gold was higher by +0.67%** last week, climbing from $1403.0 to $1412.5 (MTD +7.80%, YTD +10.23%).

HEDGE FUNDS

Hedge fund returns in June are higher for the month with core strategies Equity Hedge, Event Driven, Macro, Relative Value and Multi-Strategy all in positive territory.

Performance:

I) The HFRX Global Hedge Fund Index is higher at +1.46% MTD and up +4.08% YTD.
II) Equity Hedge has advance by +1.25% MTD and is up +5.83% YTD.
III) Event Driven is higher MTD +1.43% and is higher YTD +2.26%.
IV) Macro/CTA has risen by +2.40% MTD and is up +2.40% YTD.
V) Relative Value Arbitrage is higher by +1.06% and is up +4.11% YTD.
VI) Multi-Strategy is positive MTD at +1.05% and is higher by 3.86% YTD.

ECONOMIC DATA WATCH AND MARKET OUTLOOK

Looking ahead to the **next week of trading**, it will be interesting to see how the **markets** will **balance out expectations versus reality**. **Fed Chairman Powell** last week unnerved investors by **highlighting several risks** he saw in the global economy, including low expectations for a short-term resolution to the U.S./China trade dispute, rising tensions in Iran and slowing economic growth. But **despite** these **uncertainties**, U.S. equity markets closed out the first half of 2019 on a strong note. The **Dow Jones Industrial Average** (+7.31%) and **S&P 500** (+7.05%) posted their **best June returns since 1938 and 1955** respectively.

The seemingly **inexorable rise** in the **equity indexes** is being propelled by **investors expecting** a positive **resolution to the U.S./China trade** talks, and at least **two interest rate cuts** from the Federal Reserve in 2019. These optimist views over the **short-term** seem to have the **equity markets priced to perfection**. Even a quick resolution to the trade talks and a rate cut in July could prompt a short rally, but the risk on the downside is more pronounced. We believe a protracted trade negotiation between the U.S. and China, and less than two rates cuts from the Fed, can lead to a sharp downside move in the equity markets. As such, we **anticipate volatility to pick** up over the summer and we should be reminded of the saying "**expect the unexpected**".

In turning to **next week's economic calendar**, we will see if there have been improvements in the **manufacturing** sector and **job growth**, after a disappointing round of data in May. On **Monday**, the **ISM Manufacturing Index** for June is expected to come in at a **consensus 51.2**, which shows **modest** and slowing **growth**. This is a recovery from May's ISM manufacturing report which came in below expectations for a second month in a row at 52.1 and a three-year low.

On Tuesday, we get the report for **Motor Vehicle sales**, where the consensus for total unit vehicle sales in **June** is a **17.0 million** annual rate versus a higher-than-expected rise in May's pace to 17.3 million.

The advance report of the durables component of the **May factory orders** report fell 1.3%, though ex-transportation orders increased 0.3% while core capital goods orders rose 0.4%. Forecasters for Wednesday's report see factory orders in May, which will include initial data on non-durable goods, **falling 0.3%.** Also, out on Wednesday is the **ISM Non-Manufacturing** Index where the Street consensus sees **slowing to 55.9** versus May's stronger-than-expected 56.9. Both new orders and business activity were strong in the May report.

We finish the week with the **U.S. jobs data**, where the **consensus estimate** calls for a **solid 165,000** new jobs versus May's unexpectedly weak 75,000 gain. The **unemployment rate** is expected to **hold at 3.6%** with average hourly earnings, which were very soft in the May report, climbing back up to an increase of 0.3%. The **year-on-year rate for earnings** is expected to move **0.1% higher to 3.2%.** Private payrolls are seen rising 150,000 but with manufacturing payrolls expected to increase only 1,000. The workweek is seen rising incrementally to 34.5 hours with the **labor participation rate steady at 62.8%.**

Data Source: Haver Economics