

# Weekly Capital Market Comments

Friday, February 8, 2019

## She Loves Me, Xi Loves Me Not

### Weekly Review

Equities pulled a 180 this week. Despite moving up over 2% by Wednesday, US equity markets gave back much of the week's gains ending higher (Thursday-Thursday) by only 0.2% overall. At the same time, fixed-income indices finished the week flat-to-down, overall. Industrials outperformed from a Sector perspective, higher by 1.6%, driven up by gains in Boeing, GE and Honeywell. Trailing sectors included Consumer Cyclical, down 1.0% and Energy names, down 1.2%. From a style perspective, the Mid-Cap names continued to outperform, with Mid-Cap Growth and Core higher by 1.3% and 1.1%, respectively. Lagging was Large-Cap Growth, down by 0.1% and Large-Cap Value, off by 0.4%.

### Trading Around Trade

The market is clearly concerned that the much-anticipated trade summit between President Trump and President Xi will not occur prior to the March 1 deadline, increasing tariffs from 10% to 25% on an additional \$200bn of Chinese goods. We on the other hand believe the recent market pause was simply an excuse by investors to fade the recent rally. As we point out in our "House View – 2019 Year Ahead" presentation, we believe trade tariffs will prove to be transitory, and that neither the US nor China will benefit from a full-out trade war. While it is clear to us the US economy is decelerating, we must note that Chinese economy is in even worse shape. Despite additional monetary stimulus (further reserve requirement reductions), deregulation and tax cuts (VAT and Enterprise Tax; come March '19), the Chinese industrial and manufacturing sectors – while stabilizing – still remain challenged. In addition, retail sales seem to be declining and corporate profits are under pressure. Add to this the Chinese Lunar New Year holiday which began on February 5<sup>th</sup>, lasts primarily until the 10<sup>th</sup>. During this time, the government and commerce effectively shut down. As a result, we believe over the next week or so, the US trade delegation or President Trump will announce a delay in any additional tariffs until more high-level meetings are conducted in the next 60 days. However, the risk remains that President Trump alienates his base with more dovish positioning toward China; hence we would not be surprised of ad-hock Executive Orders helping limit IP theft/transfer commensurate with any delay announcement.

On Wednesday the S&P was trading around 16.4x forward four-quarter earnings (~\$167); the highest point since early December 2018. In addition, credit spreads contracted to the tightest level since early December 2018 as well. This, combined with several of the near-term risks we cited last week (Fed downgrading the economy, synchronized global slowdown, slowing earnings growth, a lack of any additional fiscal stimulus), we were not surprised the market paused on Thursday. Further, we fully expect investors will look for additional reasons to sell down the market in coming days. So, the recent retracement, in our opinion, was simply driven by tactical investors booking profits; this following a 9% total return in the S&P500 YTD, and a positive 12% retracement from Christmas Eve's lows. All else equal, we believe strategic investors should stay the course, continue to focus on diversified allocations with a "value-tilt" in mind. In other words, we continue to favor stocks and sectors with attractive valuations and well-capitalized balance sheets. We like cash-flow generating business that deliver predictable dividend streams. Technology and Growth have recovered nicely over the last four to five weeks, but similar to High-Yield Bonds, we look to fade these trades as well.

**We'd love to hear your thoughts.**

Domestic Indices		1Week
1	S&P MidCap 400	1.1%
2	DJ Industrial Average TR	0.8%
3	Russell 2000 TR	0.4%
4	ICE BofAML US High Yield TR	0.4%
5	BBgBarc Municipal TR USD	0.2%
6	S&P 500 TR	0.1%
7	NASDAQ Composite PR	0.1%
8	BBgBarc US Agg Bond TR	0.0%
9	BBgBarc US Government TR	0.0%
10	NYSE Composite PR	0.0%
11	US Inter Gov Bd TR Bond	-0.1%
12	BBgBarc US MBS TR	-0.1%

Style Stratification		YTD
1	US Mid Growth	1.3%
2	US Mid Core	1.1%
3	US Mid Cap	0.9%
4	US Core	0.8%
5	US Large Core	0.7%
6	US Mid Val	0.3%
7	US Market	0.2%
8	US Growth	0.2%
9	US Large Cap	0.0%
10	US Large Growth	-0.1%
11	US Large Val	-0.4%

Sector Stratification		YTD
1	US Industrials	1.6%
2	US Technology	1.2%
3	US Utilities	1.1%
4	US Real Estate	1.0%
5	US Snstve Sup Sec	0.9%
6	US Financial Services	0.4%
7	US Commun Svc Capped	0.3%
8	US Consumr Dfnsv	0.3%
9	US Cyclcl Sup Sec	-0.2%
10	US Dfnsv Sup Sec	-0.3%
11	US Healthcare	-0.9%
12	US Basic Materials	-0.9%
13	US Consumr Cyclcl	-1.0%
14	US Energy Capped	-1.2%

Bond Indices		YTD
1	ICE BofAML US High Yield TR	0.4%
2	US Lng Corp Bd TR Bond	0.3%
3	US Corp Bd TR Bond	0.2%
4	BBgBarc Municipal TR USD	0.2%
5	US Lng Core Bd TR Bond	0.2%
6	US Inter Corp Bd TR Bond	0.1%
7	US Lng Gov Bd TR Bond	0.0%
8	US Core Bd TR Bond	0.0%
9	US Shrt Gov Bd TR Bond	0.0%
10	US Gov Bd TR Bond	0.0%
11	US Inter Core Bd TR Bond	-0.1%
12	US Inter Gov Bd TR Bond	-0.1%
13	Mortgage TR Bond	-0.1%
14	US TIPS TR	-0.3%

International Markets		YTD
1	MSCI Pacific Ex Japan PR LCL	2.6%
2	FTSE 100 TR GBP	1.8%
3	MSCI Pacific PR LCL	0.8%
4	MSCI World Ex USA PR LCL	0.7%
5	SSE Composite PR CNY	0.6%
6	MSCI Europe PR LCL	0.6%
7	MSCI Japan PR LCL	-0.1%
8	Euronext Paris CAC 40 NR EUR	-0.1%
9	MSCI EM PR LCL	-0.1%
10	MSCI Pacific NR USD	-0.3%
11	MSCI World ex USA NR USD	-0.4%
12	MSCI Europe NR USD	-0.5%
13	MSCI EM PR USD	-0.8%
14	FSE DAX TR EUR	-1.3%

Source: Morningstar.com

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