THOUGHTS OF THE WEEK

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WEEKLY HEADINGS

Key Takeaways

Equity Markets Entering the 'Dog Days of Summer'

Below Average Trading Volumes Can Lead to Exacerbated Price Swings

Remain Patient and Position for Buying Opportunities

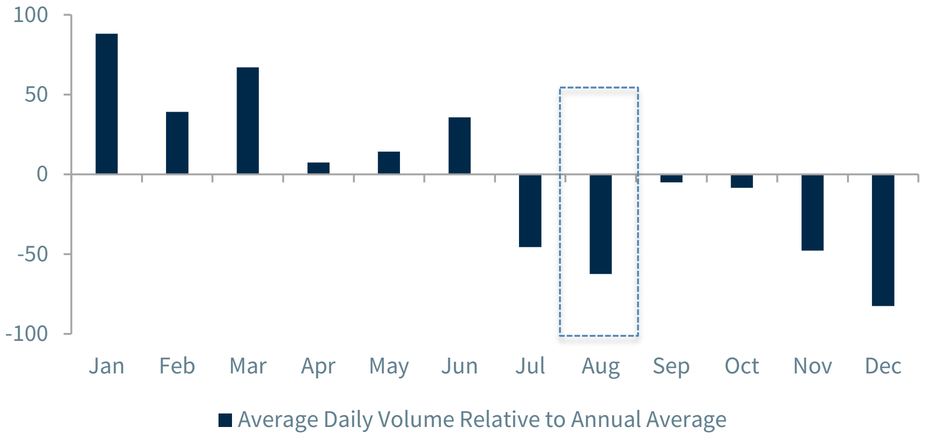
The origin of the phrase "dog days of summer" traces back to Greek astronomy. The ancient Greeks discovered a 40-day period in which Sirius, also known as the "dog star," rose and set in conjunction with the sun. Since Sirius is the brightest star in its constellation, they believed the additional glow was responsible for the scorching summer days. Greek literature expanded the myth by linking the incredibly hot part of the summer to include drought, sudden thunderstorms, and even bad luck. Today, we add another interpretation, as the 'dog days of summer' is not only applicable to the sultry summer weather, but also the current state of the financial markets.

- **Hot, Hot, Hot |** Through July 31, the S&P 500 was off to its fastest start to a year (20%) in over 20 years and its valuation (S&P 500 NTM P/E = 17.3x) rose to its highest level since March 2018. However, as we had cautioned in previous *Weekly Headings*, the equity market may have stayed in the sun a little too long as it was priced to perfection and increasingly susceptible to disappointing monetary policy, escalating trade tensions between the US and China, and unfavorable outcomes for other geopolitical risks such as Brexit and the US-Iran conflict. The recent pullback in the equity market offered a buying opportunity as it provided more palatable risk/reward prospects (See our *Thoughts on the Market* titled "Head Fake or Head Shake?" from 8/7/19). The combination of longer-term Treasury yields falling to multi-year lows (10-year Treasury yield: 1.70%), a record $15 trillion in negative-yielding debt across the globe, and the highest level of cash on the sidelines since 2010 (money market fund balances at $3.28 trillion) and the highest percentage of 'bearish' investors (contrarian indicator) over the past eight months (according to the AAII survey) enhanced the attractiveness of equities.*
- **Drought |** One of the recurring risks in the markets is that the heavy vacation season reduces the trading volume in the market. According to a recent AAA Travel survey, of the nearly 100 million Americans planning to embark on a family vacation this year, more than two-thirds booked their travel for the summer months. Therefore, it is no surprise that the month of August has the second lowest average trading volume of any month during the year (December is the lowest given the holiday season) and the longest period of days with below-average equity trading volumes. Usually, the lack of market participants is not a major problem as the mid to latter part of August does not have earnings season, major economic data, FOMC meetings (although we do have the Jackson Hole Symposium on August 22-24), and Congress is on summer recess.
- **Sudden Thunderstorms |** However, as a result of low volumes, when market moving headlines (e.g., sudden thunderstorms) hit, market moves in either direction are exacerbated by these lower volumes. Some of the thunderstorms that might pop up sporadically include President Trump tweets, US/China trade issues, and global central bank rhetoric and/or action. Our view is that investors need to ignore the 'quick changing weather' and focus on the long-term fundamentals. Our base case remains that the economy continues to be healthy and until that view changes, we have a favorable outlook for the equity market, including our favorite sectors (Technology, Consumer Discretionary, Communication Services and Health Care). For investors seeking ways to mitigate portfolios from some of these potential storms, an 'umbrella' of 'safer' investments could prove beneficial. The diversification benefit has been evident in the most recent S&P 500 decline (~6%) as gold (4.0%) and Treasuries (2.1%) significantly outperformed during this tumultuous time period (July 26 – August 5).
- **Bad Luck |** Historically, August begins a more lethargic period of time for the equity market. The August through September period has historically been the weakest rolling two-month time period for the S&P 500 (-0.6% on average) since 1980.* However, that does not mean investors should flee the market. Rather, we suggest investors remain engaged with the markets as any potential pullbacks, like the one experienced over the last few days, could provide opportunities to increase exposure to riskier assets such as equities as we head into the fourth quarter, a historically strong period for equities.

CHART OF THE WEEK

Historically, August Exhibits a Softer Trading Volume Environment

Over the past ten years, August has had the second lowest volume of any month during the year.



*See Charts of the week on page 3.

ECONOMY

- The 10% tariff on the remaining $300 billion in imports from China to the US (set to begin September 1) falls more on consumer goods than previous tranches of tariffs. However, the impact should be partly offset by China's currency devaluation.
- Chair Powell listed three reasons why the Fed cut rates in late July, and what it would focus on in deciding its next move: 1) the downside risks for weaker global growth and trade policy uncertainty; 2) the impact these factors have already had on the U.S. economy; and 3) the sub-2% trend in inflation. Developments over the last week have added to the downside risks, and the Fed is seen as more likely to lower rates at the policy meetings in mid-September or October as the federal funds futures market is pricing in a ~100% chance of a September 18 rate cut (75% of a 25 basis point (bps) cut and 25% of a 50 bps cut).*
- **Focus of the week:** Next week, there will be a number of key inflation, consumer and manufacturing indices worth monitoring. CPI is expected to be boosted slightly at the headline level to 2.1% year-over-year (YoY) by the rise in gasoline prices. This remains well above the Fed's preferred inflation gauge, PCE, which at 1.6% is stubbornly below the Fed's 2% target. For the consumer, the recent moderation in motor vehicle sales will likely weigh on retail sales. However, we have had a couple of months of strong core retail sales, so some moderation is warranted. Industrial production is expected to be largely unchanged, but there are downside pressures from idiosyncratic issues at Boeing and slowing global economic momentum.

THE WEEK AHEAD: August 12 – August 16

MON		WED	Import Prices	FRI	Building Permits
TUE	Consumer Price Index	THU	Retail Sales Jobless Claims Industrial Production	FUTURE EVENTS	8/21 FOMC Minutes 8/22-8/24 Fed Jackson Hole Economic Symposium 8/29 Real GDP (2Q19 Second Estimate)

US EQUITY

- ~89% of S&P 500 companies have reported, on average, fairly good results. The aggregate earnings surprise has been 5.3% on a 0.6% aggregate sales surprise for 2.4% earnings growth on 4.0% sales growth. Guidance has generally been more disappointing on trade uncertainty and a soft global macro environment. US-centric companies have reported better fundamentals again this quarter. For example, S&P 500 companies with over 50% of their revenues from the US have reported 4.5% earnings growth on average vs. companies with over 50% of their revenues from overseas reporting -0.9% earnings growth on average.
- Despite the sharp rally off of the lows on Monday, we caution investors from becoming overly complacent. A significant amount of uncertainty regarding trade remains, so a re-test of the recent lows remains a realistic possibility.
- **Focus of the Week:** Use pull-backs to accumulate and avoid the tendency to get too focused with market timing, since picking an absolute bottom during down-drafts is extremely difficult and a down move similar to the 19.5% draw-down last fall is unlikely. Stocks offer attractive upside over the next 12-months and we maintain our 12-month base case for the S&P 500 of 3108.

FIXED INCOME

- The 10 year/3 month Treasury spread has been inverted for 87 days now, while our preferred indicator, the 10 year/2 year Treasury spread, has narrowed significantly to 10 bps. A negative slope in the yield curve has been a sign of an economic cycle turning point, while the S&P 500 tends to peak on average nine months after the 10 year/2 year spread turns negative.*
- World interest rates continue to decline. In an attempt to advance growth, the key central banks (excluding the Fed) have not only maintained accommodative policies, but pledged continued quantitative easing programs to accelerate activity. In essence, they are printing money. Germany, Netherlands and Switzerland now have their entire yield curve (0-30yr) in negative yields. As long as inflation remains in check and central banks continue QE programs, it is likely interest rates will not rise significantly.
- **Focus of the week:** The amount of global negative-yielding debt rose more than $1 trillion in just two business days to record highs, now north of $15.6 trillion.* Negative-yielding debt is now estimated at ~27% of all world debt, and if US sovereign debt is excluded, that percentage jumps to 44%. Negative yielding bonds, are in part, a feature of continued central bank buying (through the re- investment of maturing assets) as their demand for bonds is pushing prices higher and yields lower, which is a sign of a slowing global economy. The negative yielding debt trend will continue as long as central banks push accommodative policies and future fear pushes investors from risky assets to less risky assets like Treasuries.

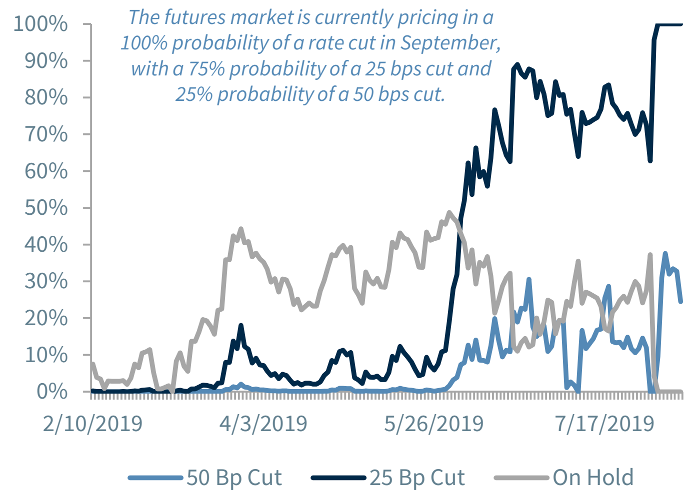
INTERNATIONAL, POLITICAL & CURRENCY

- Despite crude oil posting the largest seven-week US inventory decline on record, crude oil fell sharply to the lowest level in eight months as the escalation in the trade conflict between the US and China raised concerns regarding the health of future demand. As a result, Saudi Arabia pledged it would do whatever it takes to raise crude oil prices.
- Given the continued fall in global sovereign bond yields, rising expectations for additional accommodation from global central banks (the Fed in particular) and the continued slowdown in global economic momentum, gold has sustained its recent rally and rose above the $1,500/oz level for the first time since 2013.
- The risk of dollar exchange rate intervention continues to rise following the devaluation of the yuan to an 11-year low which sparked accusations by President Trump of "historic currency manipulation" by China. China's currency actions are a warning (and retaliation) to President Trump as the new 10% tariff on $300 billion Chinese goods will not be effective until September 1.
- **Focus of the week:** Trump has consistently demonstrated his willingness to pursue unorthodox executive authority to exert maximum pressure in trade negotiations. Officially instructing the Treasury Department to label China as a currency manipulator ahead of the Treasury's official October report does little in the near term, but opens the door to exerting further pressure on China in the future – potentially in the form of dollar devaluation. With US-China relations trending negative in the near term, the Fed's decisions gain greater importance since if they turn more accommodative, it may limit the extent to which the Trump administration seeks to reduce the strength of the dollar.

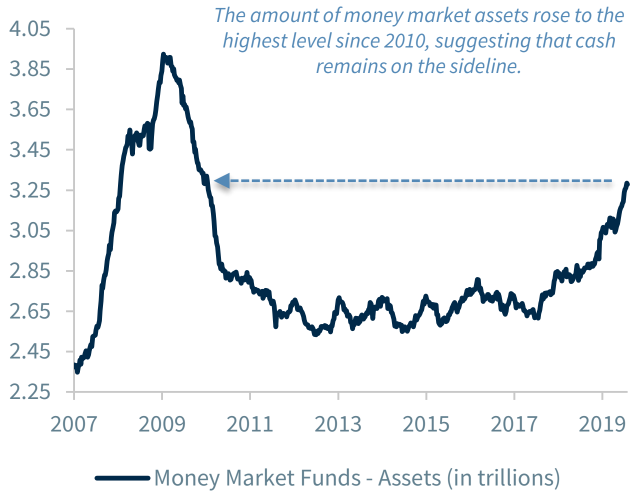
*See Charts of the week on page 3.

Charts of the Week

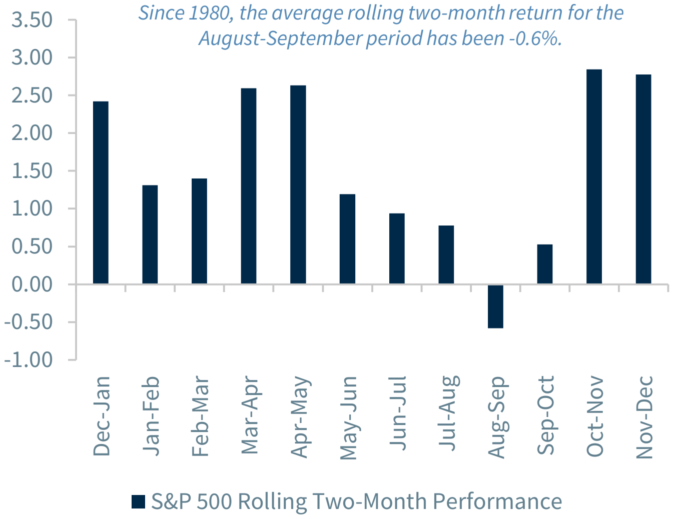
September Rate Cut Probabilities



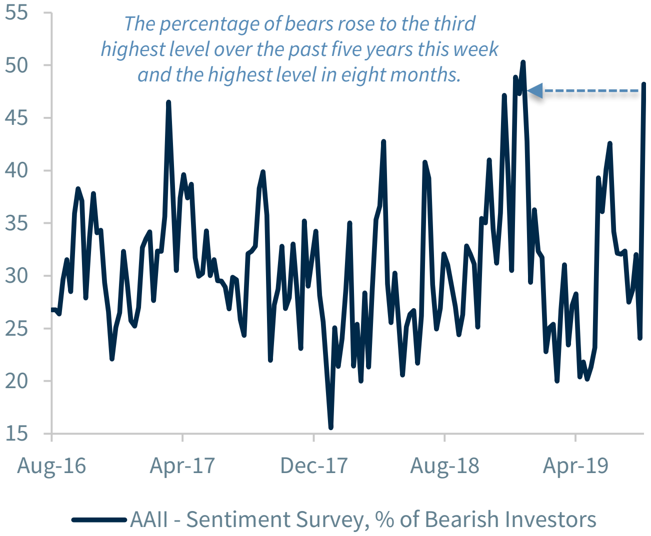
Money Market Funds Highest Since 2010



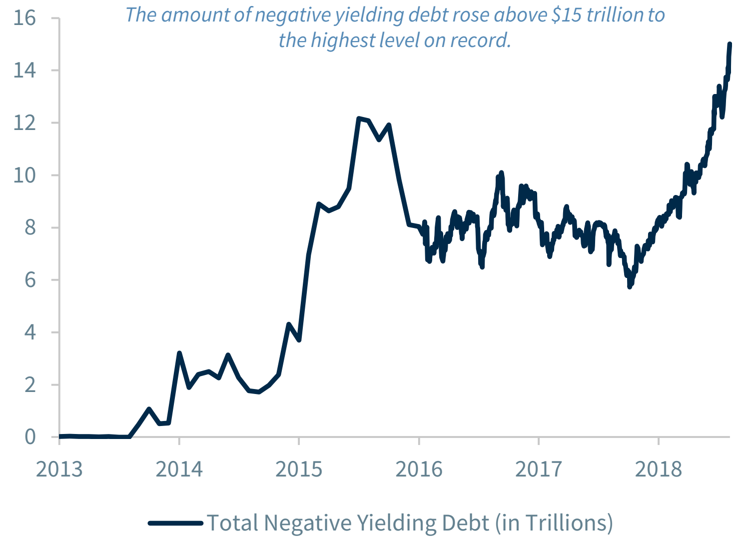
August to September Historically Weak



% of Bearish Investors Shoots Higher



Amount of Negative Yielding Debt Hits Record High



10 year/2 year Spread Slides Further

Asset Class Performance | Distribution by Asset Class and Style (as of August 8)

Weekly Returns (as of August 8)

U.S. Equities (S&P indices)

	Value	Blend	Growth
Large Cap	-0.2%	0.2%	0.6%
Mid Cap	0.3%	0.6%	0.9%
Small Cap	0.4%	0.5%	0.6%

International Equities (MSCI indices)

	Dev. Mkt	World	Emerg. Mkt
Large Cap	-1.3%	-0.4%	-1.4%
Mid Cap	-1.3%	-0.2%	-1.3%
Small Cap	-1.3%	-0.3%	-0.7%

Fixed Income (Bloomberg Barclays indices)

	1-3 YR	Medium	Long
Treasury	0.0%	0.7%	1.3%
Invest. Grade	0.2%	0.4%	0.6%
High Yield	-0.2%	-0.3%	-0.4%

Year-to-Date Returns (as of August 8)

U.S. Equities (S&P indices)

	Value	Blend	Growth
Large Cap	16.1%	18.6%	20.8%
Mid Cap	14.5%	16.9%	19.2%
Small Cap	12.1%	12.5%	13.0%

International Equities (MSCI indices)

	Dev. Mkt	World	Emerg. Mkt
Large Cap	11.4%	14.8%	5.7%
Mid Cap	11.3%	15.6%	4.2%
Small Cap	10.6%	13.5%	3.4%

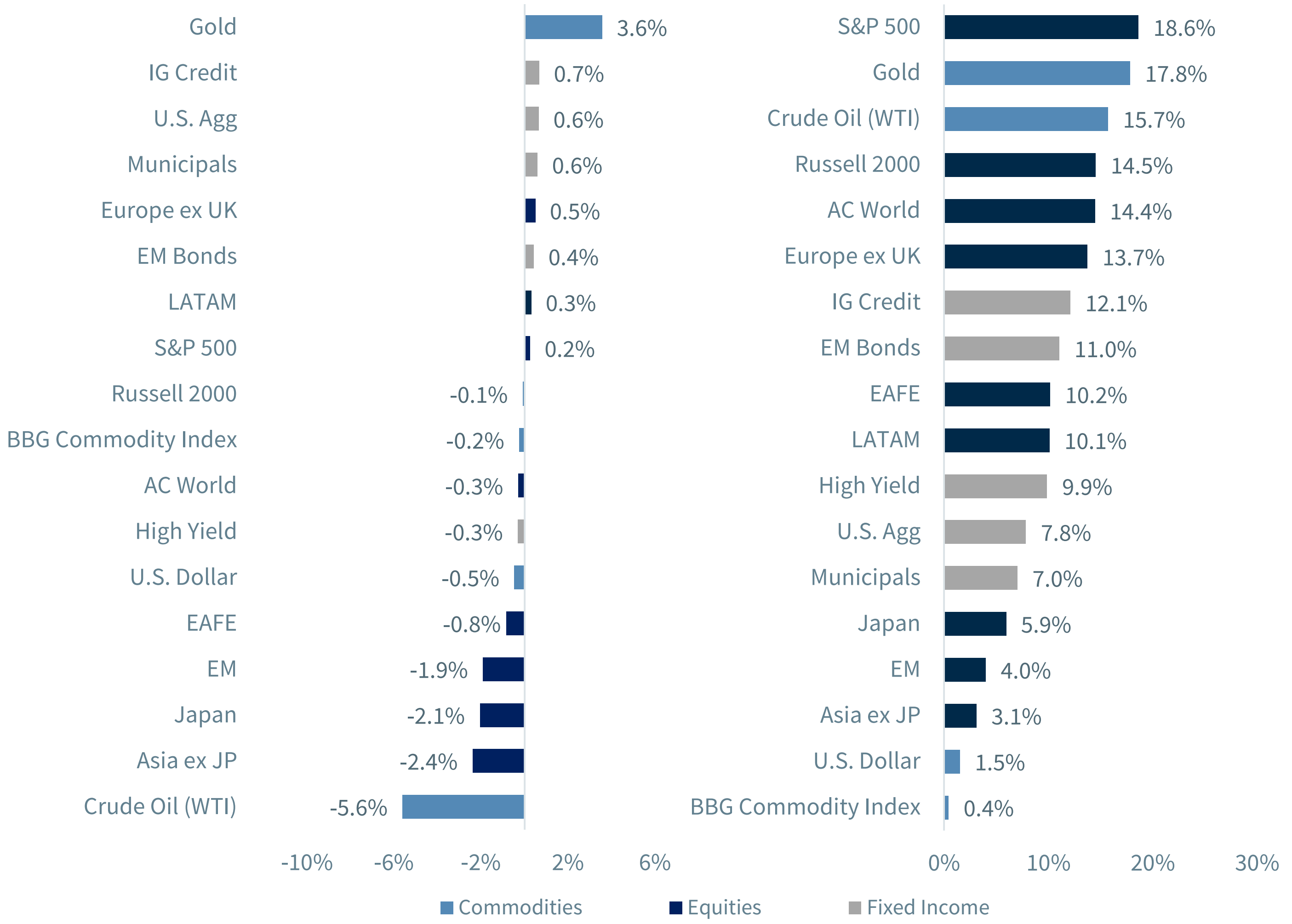
Fixed Income (Bloomberg Barclays indices)

	1-3 YR	Medium	Long
Treasury	1.5%	6.0%	10.4%
Invest. Grade	3.8%	8.3%	11.8%
High Yield	5.2%	9.6%	16.1%

Asset Class Performance | Weekly and Year-to-Date (as of August 8)

Week-to-Date**

Year-to-Date**



Assumes all asset classes are priced in US dollars unless otherwise noted. | Ranked in order of performances (best to worst).

Weekly Data

Data as of August 8

U.S Equities

Index	Price	Weekly	MTD	YTD	1 Year	3 Year	5 Year	10 Year
S&P 500	2938.1	0.2	(1.4)	18.6	4.9	12.7	10.8	15.8
DJ Industrial Average	26378.2	(0.4)	(1.8)	13.1	3.1	19.3	12.6	16.1
NASDAQ Composite Index	8039.2	0.4	(1.7)	21.2	1.9	19.9	13.1	19.0
Russell 1000	3130.2	0.3	(1.4)	19.0	8.0	13.3	11.2	14.1
Russell 2000	3807.7	(0.1)	(2.7)	14.5	(4.4)	10.4	8.5	12.5
Russell Midcap	5716.7	0.6	(1.6)	21.1	6.7	11.0	9.6	14.3

Equity Sectors

Sector	Price	Weekly	MTD	YTD	1 Year	3 Year	5 Year	10 Year
Materials	364.2	1.5	(0.3)	16.4	0.3	8.2	5.5	9.5
Industrials	639.8	0.3	(2.3)	19.3	2.1	10.4	9.7	13.8
Comm Services	167.3	0.2	(1.1)	21.7	11.8	1.7	5.7	9.9
Utilities	308.2	1.1	2.2	16.9	18.9	10.0	11.9	12.0
Consumer Discretionary	942.2	1.0	(1.2)	21.5	6.0	15.1	14.0	18.0
Consumer Staples	612.6	0.6	0.3	19.4	14.8	6.2	9.3	12.6
Health Care	1055.2	0.2	0.2	6.5	3.1	8.8	10.4	14.8
Information Technology	1392.2	0.5	(1.7)	29.1	9.4	23.0	18.7	17.6
Energy	441.5	(0.9)	(4.5)	6.2	(18.1)	(1.6)	(6.1)	3.9
Financials	451.3	(1.3)	(3.7)	15.6	(2.2)	13.9	10.6	10.9
Real Estate	238.0	1.7	2.7	25.9	20.1	8.1	10.5	14.8

Fixed Income

Index	Yield	Weekly	MTD	YTD	1 Year	3 Year	5 Year	10 Year
3-Month Treasury Bill (%)	2.0	0.0	0.1	1.5	2.3	1.4	0.9	0.5
2-Year Treasury (%)	1.6	0.2	0.6	2.8	4.2	1.3	1.1	1.2
10-Year Treasury (%)	1.7	1.3	2.8	10.4	14.2	1.6	3.2	4.5
Barclays US Corporate High Yield	6.5	(0.3)	(0.6)	9.9	5.8	6.3	5.0	8.4
Bloomberg Barclays US Aggregate	2.3	0.6	1.4	7.8	9.6	2.8	3.2	4.0
Bloomberg Barclays Municipals		0.6	1.0	7.0	8.5	3.2	3.9	4.7
Bloomberg Barclays IG Credit	3.0	0.7	1.5	12.1	12.0	4.4	4.4	5.9
Bloomberg Barclays EM Bonds	4.8	0.4	0.5	11.0	11.4	4.9	5.1	7.3

Commodities

Index	Price	Weekly	MTD	YTD	1 Year	3 Year	5 Year	10 Year
WTI Crude ($/bl)	52.5	(5.6)	(10.3)	15.7	(21.5)	6.9	(11.7)	(3.0)
Gold ($/Troy Oz)	1509.5	3.6	5.0	17.8	23.6	4.0	2.9	4.6
Dow Jones-UBS Commodity Index	77.0	(0.2)	(2.4)	0.4	(9.5)	(3.0)	(9.6)	(5.1)

Currencies

Currency	Price	Weekly	MTD	YTD	1 Year	3 Year	5 Year	10 Year
U.S. Dollar Index	97.6	(0.5)	(0.9)	1.5	2.7	0.4	3.7	2.1
U.S. Dollar per Euro	1.1	0.9	0.6	(2.0)	(3.5)	0.4	(3.5)	(2.4)
U.S. Dollar per British Pounds	1.2	0.1	(0.9)	(4.7)	(5.8)	(2.4)	(6.3)	(3.1)
Japanese Yen per U.S. Dollar	106.2	(0.3)	(2.2)	(3.2)	(4.3)	1.2	0.8	0.9

International Equities

Index	Price	Weekly	MTD	YTD	1 Year	3 Year	5 Year	10 Year
MSCI AC World	512.6	(0.3)	(2.2)	14.4	0.8	9.9	6.9	9.4
MSCI EAFE	1846.4	(0.8)	(2.6)	10.2	(3.9)	6.7	3.0	5.9
MSCI Europe ex UK	1930.3	0.5	(1.5)	13.7	(2.2)	8.4	3.7	6.2
MSCI Japan	3068.6	(2.1)	(2.0)	5.9	(6.6)	5.8	5.1	5.6
MSCI EM	984.3	(1.9)	(5.0)	4.0	(6.1)	6.1	1.5	4.3
MSCI Asia ex JP	603.9	(2.4)	(5.4)	3.1	(7.6)	6.5	3.3	6.2
MSCI LATAM	2768.5	0.3	(2.6)	10.1	5.9	7.5	(1.0)	1.0

Disclosures

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Their markets are likely to be volatile and there may be sharp price fluctuations even during periods when prices overall are rising. Gold is subject to the special risks associated with investing in precious metals, including but not limited to: price may be subject to wide fluctuation; the market is relatively limited; the sources are concentrated in countries that have the potential for instability; and the market is unregulated. The S&P 500 is an unmanaged index of 500 widely held stocks that is generally considered representative of the US stock market. The Bloomberg Barclays US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market. The risk of default may increase due to changes in the issuer's credit quality. Price changes may occur due to changes in interest rates and the liquidity of the bond. When appropriate, these bonds should only comprise a modest portion of a portfolio. The Citi Economic Surprise Indices measure data surprises relative to market expectations. The S&P 500 is an unmanaged index of 500 widely held stocks that is generally considered representative of the US stock market. The MSCI Emerging Markets is designed to measure equity market performance in 25 emerging market indices. The index's three largest industries are materials, energy, and banks. The MSCI EAFE (Europe, Australasia, and Far East) is a free float-adjusted market capitalization index that is designed to measure developed market equity performance, excluding the United States & Canada. The EAFE consists of the country indices of 22 developed nations. MSCI EM Eastern Europe Net Return Index: The index captures large and mid cap representation across 4 Emerging Markets (EM) countries in Eastern Europe. With 50 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country. MSCI Japan Net Return Index: The index is designed to measure the performance of the large and mid cap segment of the Japanese market. With 319 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in Japan. MSCI EM Asia Net Return Index: The index captures large and mid cap representation across 8 Emerging Markets countries. With 554 constituents, the index covers approximately 85% of the free float- adjusted market capitalization in each country. MSCI Europe ex UK: The MSCI Europe ex UK Index captures large and mid cap representation across 14 Developed Markets (DM) countries in Europe*. With 343 constituents, the index covers approximately 85% of the free float-adjusted market capitalization across European Developed Markets excluding the UK. MSCI Asia ex JP: The MSCI Asia ex Japan Index captures large and mid cap representation across 2 of 3 Developed Markets (DM) countries* (excluding Japan) and 9 Emerging Markets (EM) countries* in Asia. With 955 constituents, the index covers approximately 85% of the free float adjusted market capitalization in each country. MSCI LATAM: The MSCI EM Latin America ex Brazil Index includes large and mid cap representation across 4 Emerging Markets (EM) countries* in Latin America. With 55 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country. The Bloomberg Barclays Global Aggregate Negative Yielding Debt Market Value Index measures the stock of debt with yields below zero issued by governments, companies and mortgage providers around the world which are members of the Bloomberg Barclays Global Aggregate Bond Index. The Dow Jones UBS Commodity Index is a weighted index which tracks a wide range of 22 commodity futures contracts, including metals, agricultural products, energy, and livestock. The Bloomberg Barclays US Municipal Index covers the USD-denominated long-term tax exempt bond market. The index has four main sectors: state and local general obligation bonds, revenue bonds, insured bonds and prerefunded bonds. The Bloomberg Barclays US Corporate Bond Index measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD denominated securities publicly issued by US and non-US industrial, utility and financial issuers. The Bloomberg Barclays Emerging Markets Hard Currency Aggregate Index is a flagship hard currency Emerging Markets debt benchmark that includes USD-denominated debt from sovereign, quasi-sovereign, and corporate EM issuers. Russell 2000 Total Return Index: This index covers 2000 of the smallest companies in the Russell 3000 Index, which ranks the 3000 largest US companies by market capitalization. The Russell 2000 represents approximately 10% of the Russell 3000 total market capitalization. This index includes the effects of reinvested dividends. Russell 1000 Total Return Index: This index represents the 1000 largest companies in the Russell 3000 Index. This index is highly correlated with the S&P 500 Index. This index includes the effects of reinvested dividends. Russell Mid Cap Total Return Index: This index consists of the bottom 800 securities in the Russell 1000 Index as ranked by total market capitalization. This index includes the effects of reinvested dividends. The Russell Midcap Index is a market capitalization weighted index comprised of 800 publicly traded US companies with market caps of between $2 and $10 billion. The US dollar index (USDX) is a measure of the value of the US dollar relative to the value of a basket of currencies of the majority of the US's most significant trading partners. Dow Jones-UBS Commodity Index tracks prices of futures contracts on physical commodities on the commodity markets. The index is designed to minimize concentration in any one commodity or sector. Should interest rates remain unchanged, increase, or even decline, a laddered approach to fixed income investing may help reduce risk, improve yields, provide flexibility and provide shorter-term liquidity. Risks include but are not limited to: changes in interest rates, liquidity, credit quality, volatility and duration. S&P 500 Total Return Index: The index is widely regarded as the best single gauge of large-cap US equities. The Dow Jones Industrial Average (DJIA) is an index that tracks 30 large, publicly-owned companies trading on the New York Stock Exchange (NYSE) and the NASDAQ. The Nasdaq Composite Index is the market capitalization-weighted index of over 3,300 common equities listed on the Nasdaq stock exchange. An investor could lose all or a substantial amount of their investment. Investors should consider hedge funds as a supplement to an overall investment strategy. Commodities trading is generally considered speculative because of the significant potential for investment loss. Among the factors that could affect the value of the fund's investments in commodities are cyclical economic conditions, sudden political events, changes in sectors affecting a particular industry or commodity, and adverse international monetary policies. Their markets are likely to be volatile and there may be sharp price fluctuations even during periods when prices overall are rising. No investment strategy can guarantee success. There is no assurance any of the trends mentioned will continue or that any of the forecasts mentioned will occur. 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