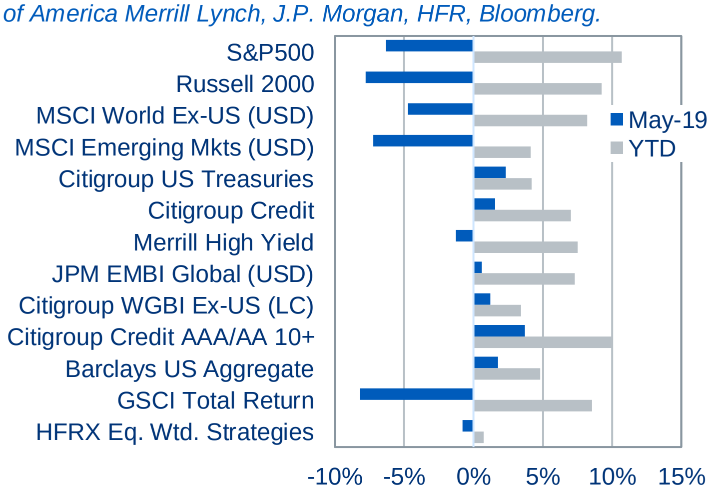
Global Market Review

Macro Summary

The skyward trajectory of global equities ended in May, as trade tensions triggered trepidations over global growth. U.S. and Chinese markets led global equity losses for the month. Advanced economy sovereign bond yields fell precipitously as investors sought safe havens, sending the yield on 10-year German bonds to a record level of negativity. The U.S. yield curve inverted, with the three-month yield exceeding the yield on the 10-year by 21 basis points, the steepest inversion since 2007. Anticipating slower growth and inflation, markets began to anticipate Fed cuts rather than further hikes. Oil erased half of the year's previous strong gains. Gold prices rose.

Performance of Major Market Indices

Sources: S&P, MSCI, FTSE Russell, Barclays, Citigroup, Bank of America Merrill Lynch, J.P. Morgan, HFR, Bloomberg.



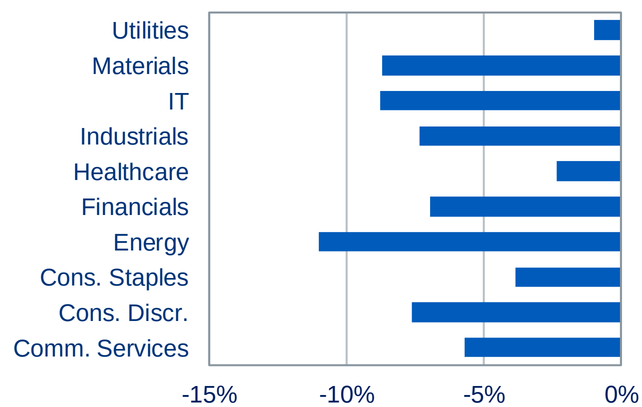
Tariff Tweet Sends Stocks Tumbling

U.S. equities tumbled in May as U.S. trade tensions soured on one front and reemerged on another. U.S.-China negotiations turned ugly mid-way through the month with China threatening to retaliate against new U.S. measures. Closer to home, on the final trading day of May, President Trump tweeted threats of new tariffs on Mexico to stem immigration across the southern U.S. border. With markets already on shaky ground, these renewed tensions with its third largest trading partner led U.S. stocks another 1% lower, sending the Russell 3000 Index down 6.5% for the month.

Trade-sensitive sectors like technology, materials, and energy led the rout within U.S. equities, while utilities, healthcare, and consumer staples suffered modest losses (Exhibit below). Small cap stocks also lagged, ending May 1.4% behind their large cap counterparts. Although trade concerns were top of mind for investors in May, signs were positive from elsewhere in the U.S. economy. Following robust GDP growth in the first quarter, both consumer spending and consumer sentiment rose in April amid better-than-expected wage growth.

Trade-Focused Sectors Bear Brunt of Losses

Source: MSCI, Bloomberg. May 2019 returns.



Global Equities Also Fall

With the U.S. at the epicenter of the trade concerns that marred global equities in May, developed non-U.S. markets fell somewhat less sharply. The MSCI ACWI ex-U.S. Index was down 4.7% in May.

1001 Nineteenth Street North
16th Floor
Arlington, VA 22209 USA

+1 703.243.4433 TEL
+1 703.243.2266 FAX

strategicgroup.com

The outlook for European growth continued its downward trend as the European Commission lowered its forecast for German growth to 0.5% from 1.1%. Political developments in Italy compounded concerns for the Eurozone as elections during the month strengthened the position of the country's new populist government. Italy's Deputy Prime Minister Matteo Salvini has challenged EU limits on government debt and spending and is poised to set the country on another collision course with Brussels over its fiscal policies. The MSCI Europe Index fell 5.5% in May.

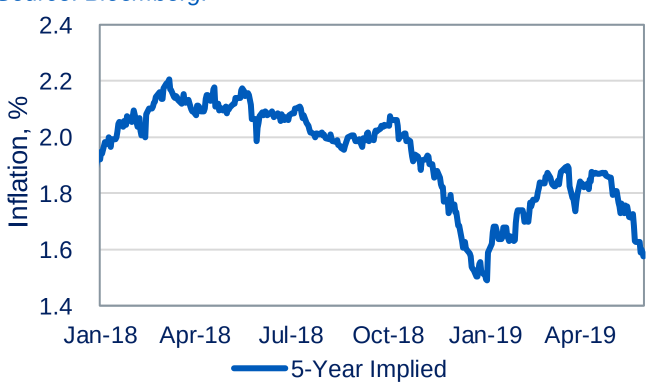
As trade negotiations soured with the U.S., Chinese equities fared the worst of global markets. The MSCI China Index lost 13% during the month. The Chinese market had experienced a resurgent start to the year, outpacing all other major markets, as the government turned to accommodative policies and trade talks with the U.S. appeared to be nearing an end. That trend took a turn in May as relations between the two largest global economies seem as far from an agreement as ever.

Yields on Safe Havens Plummet

Worsening trade tensions during the month exacerbated concerns over global growth and drove investors into safe haven assets across developed markets. Long-maturity U.S. Treasuries gained 6.6% in May and now have earned nearly 10% for the year to date. The yield on the 10-year U.S. Treasury fell to its lowest level since 2017 while the equivalent German yield reached record lows of minus 0.21%.

Inflation Expectations Fall

Source: Bloomberg.

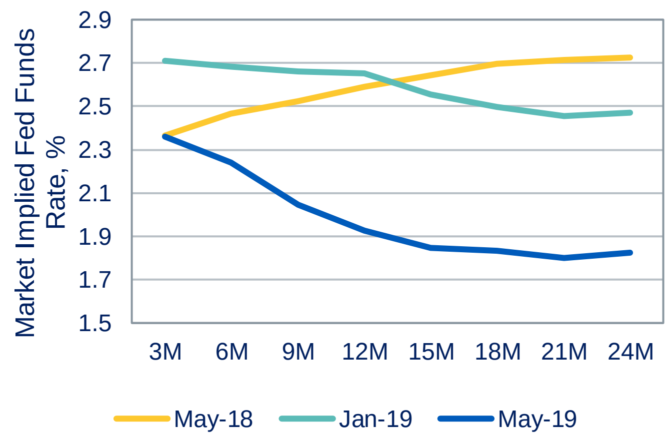


The fractious state of global trade sent expectations for global growth and inflation lower. The average inflation rate over the next five years implied by the spread between nominal and real U.S. Treasuries fell sharply (Exhibit above). Investors have begun to wonder whether the Fed may now have to cut rates rather than raise them. This is a radical shift in sentiment. Last year, futures on 3-month U.S. interest rates implied rising short-term yields. At end-May, interest rate futures markets were pricing in declining short-term rates over the next 12-18 months (Exhibit below).

Investment grade credit also benefitted from the equity rout, as long maturity U.S. corporate bonds gained 3.7% in May. High yield bonds, however, fell along with other risk assets, losing 1.3%.

Market Expectations for Fed Funds Rate Have Fallen

Source: Bloomberg.



Equity, Macro Lead Broad Losses for HFs

Losses within hedge funds were led by long/short equity and global macro strategies, hurt by falling global equities and precipitous moves in interest rates and commodity prices. Both strategies fell over 2%. Most other strategies experienced modest losses. Only relative value was able to eke out a gain in May, rising 0.2%. The HFRX Equal Weighted Index dropped 0.8% for the month.

Oil Falls on Trade, Delayed Sanctions

Oil prices declined 16% in May after consistent gains throughout the first quarter. After falling nearly 8% through May 29 as U.S.-Sino trade disputes spurred demand concerns and high U.S. inventories pointed to a supply glut, WTI Crude plunged another 8% over the last two days of the month. This further decline was sparked by the decision of the U.S. to delay the imposition of new sanctions on Iran, allowing foreign countries to continue buying Iranian petrochemical products for the near future. Gold prices rose on safe haven flows and declining yields, reaching a two-month high. The GSCI fell 8.2% in May.

Performance of Major Market Indices through 5-31-2019

Sources: MSCI, FTSE, Barclays, Citigroup, Bank of America Merrill Lynch, J.P. Morgan, S&P GSCI, HFR, Bloomberg.

	1-Month	QTD	YTD	1-Year	3-Year	5-Year
S&P500	-6.4%	-2.6%	10.7%	3.8%	11.7%	9.7%
Russell 2000	-7.8%	-4.6%	9.3%	-9.0%	9.8%	6.7%
MSCI World Ex-US (USD)	-4.7%	-2.0%	8.2%	-5.4%	5.8%	1.2%
MSCI Emerging Mkts (USD)	-7.3%	-5.3%	4.1%	-8.7%	9.9%	1.8%
Citigroup US Treasuries	2.3%	2.1%	4.2%	6.2%	1.8%	2.3%
Citigroup Credit	1.6%	2.0%	7.0%	7.4%	3.8%	3.5%
Merrill High Yield	-1.3%	0.1%	7.5%	5.4%	7.1%	4.4%
JPM EMBI Global (USD)	0.6%	0.7%	7.3%	6.9%	4.9%	4.0%
Citigroup WGBI Ex-US (LC)	1.2%	0.9%	3.4%	4.3%	1.5%	3.3%
Citigroup Credit AAA/AA 10+	3.7%	3.1%	10.0%	11.0%	5.0%	6.0%
Barclays US Aggregate	1.8%	1.8%	4.8%	6.4%	2.5%	2.7%
GSCI Total Return	-8.2%	-5.6%	8.5%	-14.1%	0.1%	-13.7%
HFRX Eq. Wtd. Strategies	-0.8%	-0.3%	0.7%	-3.8%	1.2%	0.1%