MONTHLY
MARKET REVIEW

07 2019

Strategic Investment Group®

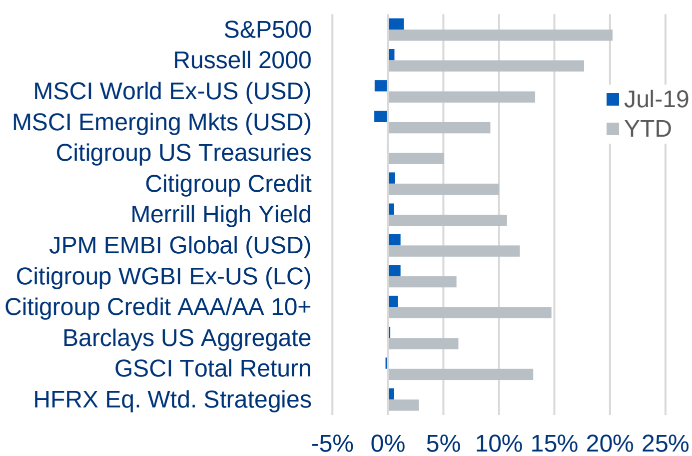
Global Market Review

Macro Summary

U.S. equity markets rose modestly in July while non-U.S. markets lost ground. Positive early earnings results and easy financial conditions were offset by Brexit chaos, sluggish growth in Europe, falling manufacturing output and trade flows, and rising trade tensions. The Fed cut rates for the first time since the Great Financial Crisis, but cautioned against expecting further easing. The ECB signaled that it too was planning a monetary stimulus package. Corporate credit and emerging debt continued to benefit from falling yields on safe haven assets. Commodities had a volatile month, but ended flat. The dollar rose.

Performance of Major Market Indices

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



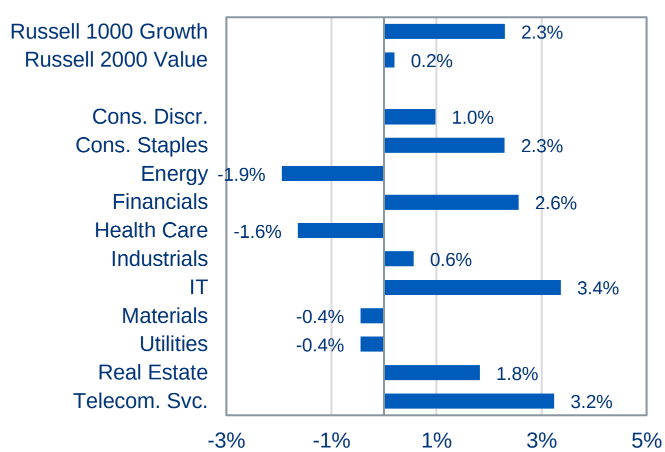
Fed Punchline Dents Equity Rally

U.S. equities finished up in July, but stumbled to the finish line after the Fed signaled a more cautious approach to easing than many had hoped. After a strong first half of the year, the S&P 500 Index rose a modest 1.4% in July. Promising early earnings results and hopes for sustained Fed easing initially propelled major U.S. indices to new highs. Blue chip tech stocks led gains for the month with companies like Alphabet jumping over 10% after reporting better-than-expected earnings. Solid second quarter GDP growth also supported equities. However, Fed Chair Powell's announcement that July's rate cut was not the harbinger of a prolonged easing cycle erased over 1% of the month's gains for the S&P 500.

So far this year, U.S. equity returns have been widely dispersed across sectors and styles (Exhibit below). Large cap and growth stocks, and in particular heavy-hitting tech companies, significantly outperformed small, value-oriented equities. Among sectors, energy and materials lost ground in the wake of heightened trade tensions and volatility in the oil market. Healthcare stocks sank 1.6% as discussions of "Medicare for All" increased policy uncertainty for the sector. Tech and telecom shares led gains within U.S. equities, each earning over 3% in July.

Tech Sector Propels Large Cap Growth Stocks Higher

Source: MSCI, Bloomberg. July 2019.



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Brexit and Trade Concerns Reignite

Global equities ended July down about 1.2% in both developed and emerging markets. Sluggish economic growth, falling manufacturing output, declining global trade flows, and the increasingly likely prospect of a no-deal Brexit weighed heavily on investor sentiment in Europe, notwithstanding promised monetary stimulus from the ECB. Emerging equity markets, and especially those in Asia, were also buffeted by falling global trade flows and the prospect for further intensifying trade tensions. Dollar strength posed an additional headwind.

With Boris Johnson – the UK's new Prime Minister – at the helm of the Brexit transition, concerns heightened over the increasing chance of a no-deal Brexit on October 31. U.K. equity markets fell 1.8% in July, while sterling lost 3.4% and currency volatility spiked. Brexit concerns compounded worries over sluggish economic growth elsewhere in Europe, sending the MSCI Europe Index down 1.9% in July, despite the ECB's promise to ease monetary conditions further.

Emerging markets declined 1.2% in July, with losses spurred mainly by threats of additional tariffs, increased volatility in the oil market, and an appreciating U.S. dollar. Protests in Hong Kong over the prospect of extraditions to mainland China further undermined sentiment.

Yield Search Drives Credit and EM Debt

Returns across fixed income markets were mixed in July as investors weighed falling yields on safe haven assets against heightened economic and political uncertainty. In a move widely anticipated by investors, the Fed cut interest rates by a quarter of a percent and announced that it would end the reduction of its $3.8 trillion balance sheet two months earlier than planned. The yield on the benchmark 10-year Treasury bond dipped following the announcement, ending the month at 2.02%. The U.S. yield curve remained inverted.

As Sovereign Yields Fall, EM and Credit Benefit

Source: Bloomberg.

The dollar gained nearly 2% against other major currencies, despite the Fed's rate cut, as yields across developed safe haven assets look even less attractive than those in the U.S. Bonds totaling $14 trillion, including the vast bulk of government bond in Europe and Japan, are priced to have negative yields. The European Central Bank announced that it would keep its key interest rate below zero. Investors expect the need for more monetary easing to stem falling growth, further depressing bond yields. The 10-year German bund yield slipped to -0.44%, with the yield curve inverted between the 1-month and 10-year maturities. Meanwhile, demand for bonds in the UK rose, driven by investors seeking safe-haven assets as the risk of a no-deal Brexit increased.

Seeking yield that is nowhere to be found in sovereign bonds across developed markets, investors continue to look toward riskier credit and emerging markets (Exhibit above). Credit markets rallied across developed regions, with spreads on European investment grade bonds more than halving so far this year, while U.S. AAA/AA+ bonds appreciated 0.9% during the month. Elsewhere, emerging market bonds rose 1.2% in July, bringing its year-to-date gains to 11.9%. Issuance across emerging markets remains robust, with policymakers seeking to take advantage of the opportunity to issue inexpensive debt.

HFs Gain amid Mixed Global Markets

Hedge funds fared quite well in the midst of mixed global equity returns. Equity market neutral was the lone negative strategy for July, ending the month down 0.7%. More beta-driven equity strategies gained over 1%, riding the rally of blue chip tech in the U.S. market. Global macro strategies rose nearly 2% for the month as yields moved across developed economies on the prospect of dovish shifts by central banks. The HFRX Equal Weighted Index rose 0.6% in July.

Iran Tensions Escalate

After a volatile month, commodity prices ended little changed in July. Tensions between Iran and the west escalated further as Iran seized two UK tankers in the Straits of Hormuz, raising fears that oil traffic in this strategic waterway would be disrupted. Crude ended the month up slightly, as abundant supply and falling global growth moderated the impact of rising geopolitical tensions. Gold prices continued to firm reflecting falling yields and heightened geopolitical uncertainty. The broad GSCI index lost a modest 0.2% in July.

Performance of Major Market Indices through 7-31-2019

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	1.4%	1.4%	20.2%	8.0%	13.4%	11.3%
Russell 2000	0.6%	0.6%	17.7%	-4.4%	10.4%	8.5%
MSCI World Ex-US (USD)	-1.2%	-1.2%	13.3%	-2.3%	6.8%	2.2%
MSCI Emerging Mkts (USD)	-1.2%	-1.2%	9.2%	-2.2%	8.4%	1.8%
Citigroup US Treasuries	-0.1%	-0.1%	5.1%	7.5%	1.2%	2.5%
Citigroup Credit	0.7%	0.7%	10.0%	10.3%	3.5%	4.1%
Merrill High Yield	0.5%	0.5%	10.7%	6.9%	6.8%	5.1%
JPM EMBI Global (USD)	1.2%	1.2%	11.9%	10.3%	4.5%	4.7%
Citigroup WGBI Ex-US (LC)	1.1%	1.1%	6.2%	7.0%	1.6%	3.6%
Citigroup Credit AAA/AA 10+	0.9%	0.9%	14.7%	15.7%	4.3%	6.8%
Barclays US Aggregate	0.2%	0.2%	6.3%	8.1%	2.2%	3.0%
GSCI Total Return	-0.2%	-0.2%	13.1%	-8.4%	4.9%	-12.4%
HFRX Eq. Wtd. Strategies	0.6%	0.6%	2.8%	-1.5%	1.3%	0.5%