GREYCOURT

Capital Market Flash Report

July 2019 A first rate cut that causes stock markets to fall, the yield curve to flatten, commodity prices to decline, and the US dollar to surge can hardly be deemed a success by the Federal Reserve. Instead of signaling commitment and resolve to engage in sustained stimulus that promotes global growth and stability, the Fed instead placed downward pressure on the global economy and tightened financial conditions by substantially strengthening the US dollar. With two FOMC members dissenting, investors should be wary.

US EQUITY

Material growth in consumer spending, over three-quarters of S&P 500 companies reporting earnings that exceeded analysts' estimates, and expectations the Fed would engage in sustained easing, pushed stocks to new highs during July. Disappointed by Jay Powell's characterization of the Fed's first rate cut as a "mid-cycle adjustment," investors hit stocks hard causing the largest one-day drop for the S&P 500 in over two months. For the month, large cap outperformed small cap, growth outpaced value, and cyclical sectors dominated defensive sectors.

	Month (%)	YTD (%)
S&P 500	1.4	21.3
Russell 1000	1.6	21.8
Russell 1000 Value	0.8	18.1
Russell 1000 Growth	2.3	25.4
Russell 2000	0.6	18.6
Russell 2000 Value	0.2	14.2
Russell 2000 Growth	1.0	22.9

NON-US EQUITY

Non-US developed stock markets increased modestly on a local currency basis but declined in US dollar terms given significant weakness in the euro and yen. European data flashed yellow as French and German PMI readings reached their lowest levels in six and one-half years. While dovish central bank policies have helped EM debt investors, trade uncertainties and anemic earnings have clouded the picture for stock buyers. The Ruihua accounting scandal in China that is disrupting new listings is certainly not helping.

	Month (%)	YTD (%)
MSCI All-Country World ex-US	-1.2	13.1
MSCI EAFE	-1.3	13.6
MSCI Europe	-1.9	14.7
MSCI Japan	0.1	8.8
MSCI Emerging Markets	-1.1	9.9
MSCI BRIC Index	-0.8	13.5

FIXED INCOME

The Fed was unable to sway bond investors with its first policy rate cut. Investors sold shorter duration US Treasury notes and bought longer maturity government bonds. The message was clear: rates investors believe that economic growth and inflation will ratchet lower. With greater than 40% of global investment grade bond markets (ex-US) trading at negative yields, current pricing is not sustainable. Interestingly, many BBB US issuers are improving their balance sheets. Municipal demand remains very high.

	Month (%)	YTD (%)
U.S. Intermediate Treasuries	-0.2	4.0
U.S. Long Treasuries	0.2	11.6
U.S. TIPS	0.4	6.7
Corporate IG Bonds	0.3	8.7
High-Yield Bonds	0.6	10.7
Tax-Exempt Bonds	0.8	6.0

CURRENCIES

The Fed sent an ambiguous signal regarding its commitment to aggressively deploy rate cuts that will encourage growth and reflation. Currency markets responded by zeroing in on likely future interest rate differentials, and selling off the euro, pound, yen, and most emerging markets currencies. With central bankers already synchronizing monetary stimulus actions, the strengthening US dollar and flattening US yield curve revealed investor demand worldwide for additional central bank intervention.

	Month (%)	YTD (%)
US Dollar	2.5	2.2
Euro	-2.6	-3.2
Yen	-0.8	1.4
Emerging Markets[1]	0.0	2.3

REAL ASSETS

Countering long-standing market concerns about oil supplies, crude prices increased modestly, given several geopolitical hotspots, after stockpiles touched an eight-month low. Low inventories of nickel helped push industrial metals higher, while central banks continued to purchase gold in record volumes during a period of considerable growth and trade uncertainty. REITs appreciated as US interest rates declined. The increase in pending home sales helped offset concerns about falling mortgage applications.

	Month (%)	YTD (%)
Commodities[2]	-0.7	3.2
Energy	0.1	7.7
Industrial Metals	1.4	5.5
Gold	1.0	11.0
Master Limited Partnerships[3]	-0.2	18.5
Real Estate Investment Trusts[4]	1.3	19.6

HEDGE STRATEGIES

Gross exposure for directional equity funds rose higher this month, revealing manager conviction in current positions through what has been a period of low volatility. Net exposure, however, has fallen suggesting that sector and security selection will drive future performance. The primary prospective risk is episodic volatility that would require deleveraging and exits from crowded trades. A lack of dispersion continues to hamper market neutral managers. M&A activity helped event driven strategies.

	Month (%)	YTD (%)
Equity Hedge	1.3	7.7
Equity Market Neutral	-0.5	-1.2
Event Driven	0.2	3.6
Relative Value Arbitrage	0.4	4.5
Macro	1.8	4.4

Data Source: Bloomberg. MSCI returns are gross USD. Currency returns are Simple Price Appreciation (SPA) USD basis. Fixed Income reported on Bloomberg Barclays Indices. [1]MSCI Emerging Markets Currency Index. [2]Bloomberg Commodity Indices. [3]Alerian MLP Index. [4]FTSE NAREIT Equity REIT Index. Hedge Strategies reported on HFRX Indices SPA with one-day lag. For complete Index Descriptions, see http://www.greycourt.com/indices.html