This Week in the Market
5-20-19

Going Beyond Tariffs

Markets continued to grind lower this week as the scope of the trade war expanded. With the blacklisting of Huawei Technologies and no clear sense of when trade talks could resume, markets are beginning to price for a prolonged period of tension. In some regards, this dispute is becoming less about specific trade policies and more about the perceived Chinese threat to US dominance. With the continued disruption in trade relations and the mounting uncertainty that has resulted, US and global economic data is once again softening.

The IHS market US manufacturing PMI slowed to its slowest pace of expansion since September of 2009. In addition, CapEX has begun to decline on a month-to-month basis and decelerate year-over-year. As we've said for some time, CapEx is an important part of the equation that would allow for a prolonged business cycle. We've seen gains in productivity and it would be disappointing to see those slip as the trade war lengthens. Even with some of these indicators flashing yellow, we still need to keep perspective. The basic fabric of a strong economy are intact. Unemployment is low, wages are rising, inflation is low, and GDP is still running above trend. This fabric will start to fray the longer the trade dispute goes on, but we have time to work.

All things considered, the market is hanging in better than we might expect, given such rough headlines. Selling pressure has not been overwhelming and a pure risk-off trade hasn't taken hold in the equity market. Pockets of cyclical names continue to perform on their own merits. Bonds are a different story however, with US 10 year yields breaking to a new 52 week low. The bond market is saying that the global growth story is in trouble without a trade deal. The equity market hasn't quite come around to that narrative. Trade leveraged industries are obviously taking a hit, but you don't have to look far to find a company executing on strategy and being rewarded by the market. The Fed's latest minutes also confirmed their data driven approach which has lent support to stock prices intermittently.

To that end, stock picking is driving outperformance for our strategies against the S&P. Just a few good names like CSCO, APD, and PAYX are responsible for the bulk of our growing YTD gap against the market. We should find comfort that our portfolios are acting exactly as we've designed them to in this most recent bout of volatility.