ClarkCapital MANAGEMENT GROUP

Navigator® Market Update

K. Sean Clark, CFA, Chief Investment Officer

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K. Sean Clark, CFA®
Chief Investment Officer

As Clark Capital's Chief Investment Officer, Sean oversees all of the Firm's investment activities and heads the Firm's portfolio team. Sean joined the Firm in 1993 and is responsible for asset allocation and investment selection for Navigator Investment Solutions as well as directing ongoing market research and contributing to the development of proprietary products. Sean is a member of the Clark Capital Board of Directors, the Investment Committee and the Management Committee. He graduated from the University of Delaware, earning a B.S. and an M.A. in Economics. Sean is a Chartered Financial Analyst and a member of the CFA Institute (formerly AIMR) and the Financial Analysts of Philadelphia, Inc. Sean is considered an industry expert and is often asked to appear on CNBC and Bloomberg television to share his views on the market. In addition, Sean has been featured in a number of articles in nationally distributed business journals and newspapers.

TRADE WAR OR TIT FOR TAT?

Tensions have risen between the U.S. and China as both nations have proposed implementing tariffs as they jockey for position in ongoing trade negotiations. The tariffs originated in a U.S. effort to stem the nearly $500 billion trade deficit in goods with China. In fact, President Trump announced his desire to cut that deficit by $100 billion, a tall order given the interdependency of the two economies. The U.S. initially announced $3 billion worth of tariffs on Chinese imports, to which the Chinese appropriately responded with $3 billion of tariffs on U.S. made goods.

According to BlackRock: “Recent U.S. negotiating tactics have followed a consistent pattern: headline announcements spooking markets, followed by compromises and narrow implementation. Most major U.S. trading partners are now exempt from what were initially global steel and aluminum tariffs. U.S. President Donald Trump's tariffs on Chinese goods triggered another bout of market volatility. Yet the order contained no immediate action and left the door open for talks.”[1]

Tensions escalated further on Tuesday (4/3/18) as the Trump administration published a list of about 1,300 Chinese exports that could be targeted for a 25% tariff. These new tariffs would amount to about $50 billion worth of Chinese goods. China responded in-kind, announcing their own 25% tariff on about $50 billion of additional U.S. products including soybeans, cars, and chemicals. The Chinese response was quick, coming less than 24 hours after the U.S. announcement. China is positioning themselves as responding to U.S. aggression rather than taking a lead in punishing the U.S. In a statement, the Chinese embassy in the United States said, “As the Chinese saying goes, it is only polite to reciprocate,” adding that China intends to pursue the matter with the World Trade Organization and enact “corresponding measures of equal scale and strength against U.S. products.”

The trade showdown between Washington and Beijing has rattled investors and fueled market fears that the dispute could soon spiral into a full-blown trade war. As of right now, a full-blown trade war is not our expectation. In fact, the tariffs won't go into effect immediately, allowing time for negotiations. The administration will hold a public hearing for U.S. businesses on May 15th. Even after that, it's not clear when the tariffs would be applied.

All the bluster back and forth has added an element of uncertainty and caused additional volatility, with equity markets selling off after each U.S. announcement and countermove by China. However, the volatility has so far been contained in the equity markets and has not spilled over into a broader risk-off trade. For example, 10-year Treasury yields have only declined by 18 bps since peaking on February 21st. In addition, high yield credit spreads have only increased by 46 bps since January 26th.

Finally, coming into this year, we stated, "Following last year's unprecedented streak without any meaningful corrections and the lack of volatility, we expect to see an upturn in volatility and a return of more normal market corrections. Since we don't see a recession on the horizon, any correction should be shorter and shallower and set the market up for additional gains." The fundamental backdrop remains solid with the synchronized global economic expansion intact, the Conference Board's Leading Indicators Index at a new high, and jobless claims at their lowest levels since 1969! The correction in stocks has caused investor sentiment to sour to the point of pessimistic extremes and on the valuation front, the S&P 500 forward P/E ratio sits at 15.9, a level not seen since the Brexit event in 2016.

Given our expectation that a full blown trade war will be avoided and solid economic and earnings growth and attractive valuations and sentiment levels, we continue to believe the recent volatility is a trading correction within an ongoing bull market.

[1]BlackRock. Available at www.blackrockblog.com/2018/04/03/us-china-trade-tensions/