Clark Capital Management Group

Benchmark Review
& Monthly Recap

Highlights

- The S&P 500 Index achieved a new all-time high in July, eclipsing the 3,000 mark for the first time in history.
- As U.S. equity markets continued to advance, international stocks moved lower. The U.S. dollar rallied in July to its strongest level since the first half of 2017 and created a significant headwind for non-U.S. dollar holdings.
- The 10-year U.S. Treasury yield traded below 2% early in July, but moved back above that level for most of the month. However, it slipped lower as July progressed and closed the month at 2.02%.
- As measured by the difference between the 10-year U.S. Treasury and 3-month T-Bill yields, the yield curve flattened during July and for one day, moved into a positive sloped position. However, the inversion resumed and the month closed back in an inverted yield curve position.
- The current economic expansion in the U.S. is the longest on record passing the 10-year mark. Based on current economic data, we continue to expect ongoing economic growth through 2019 and into 2020.
- For the first time since 2008, the Fed cut interest rates in July. Although this cut was well telegraphed, the market reacted negatively as Chairman Powell dampened expectations that this cut was the beginning of an extended rate-cut cycle.

Fed Acts, Markets React

Equity Markets

The S&P 500 Index achieved a new all-time high in July and broke above the 3,000 level for the first time in its history. The momentum from June continued in July as the market's recovery from the May sell-off, which was triggered by a negative turn in the China trade negotiations, kept going. Although trade issues remained unresolved, they were trumped by rising expectations of a more accommodative Fed and a likely rate cut in July, which indeed occurred.

Most major U.S. equity indices gained in July, but international stocks could not overcome U.S. dollar strength and declined during the month. It is worth noting that although U.S. equity indices posted gains for the month, a portion of those gains were lost on July 31 following the FOMC meeting as equities sold off sharply to close out the day.

The numbers for July were as follows: The S&P 500 gained 1.44%, the Dow Jones Industrial Average (DJIA) rose by 1.12%, the NASDAQ Composite advanced 2.15%, and the Russell 2000 Index, a measure of small-cap companies, edged higher by 0.58%. Large-cap value stocks, as measured by the Russell 1000 Value Index, lagged their growth counterparts once again in July with an advance of 0.83%.

Comparatively, large-cap growth stocks, as measured by the Russell 1000 Growth Index, advanced 2.26%. Although this continues to be a challenging period for managers using value characteristics, we believe the value/growth relationship continues to become more and more stretched and over the long-term, value companies will be rewarded once again.

International equities slipped lower in July. Despite the anticipated and ultimate rate cut by the Fed during the month, the rest of the world remains more accommodative than the U.S. on a relative basis and the U.S. dollar rallied. In fact, the U.S. dollar index rose to its highest level in more than two years in July. With this backdrop, emerging market equities, as measured by the MSCI Emerging Markets Index, fell by -1.22% in July and the MSCI ACWI ex USA Index, a broad measure of international equities, declined -1.21% for the month. Year-to-date returns have still been solid for international stocks, but in general, they have not been able to keep pace with U.S. equities so far this year.

Fixed Income

The 10-year U.S. Treasury yield has dropped dramatically so far in 2019. The yield ended June at 2.0%, and early in the month (July 2nd and 3rd), it closed below the 2% mark for the first time since 2016. Although it bounced up from those lows as the month progressed, it slid lower later on in the month and ended July at 2.02%. (Quick update: Following the FOMC meeting on July 31st, the 10-year U.S. Treasury yield dropped dramatically below the 2% mark at the beginning of August.)

The Fed is trying to engineer a challenging balancing act by supporting economic growth but at the same time, not cutting rates too much too soon. Markets will continue to monitor any information from the Fed closely as investors try to figure out the pending course of Fed action. The situation seems to be complicated by ongoing pressure from the Trump administration to cut rates, which should, by definition, not be a consideration as the independent Fed determines policy action.

The yield-curve inversion (comparing the 10-year U.S. Treasury and 3-month T-bill yields) shallowed in July and had a brief day back in a positive position. However, the yield curve inversion resumed from that point and ended the month back in inverted territory. History shows us that the length of the inversion matters, and the yield curve has been in that position for the most part since late May.

We acknowledge that an inverted yield curve has historically been a negative signal for the direction of the U.S. economy. At the same time, other economic readings that tend to be on the front end of the economy, like the leading economic indicators index and job market data, are not showing the same cautionary signals. We continue to monitor developments in this area closely, but we believe economic growth will continue through 2019 and into 2020.

In this environment, fixed income results were as follows: The Bloomberg Barclays U.S. Aggregate Bond Index was up 0.22% for the month, the Bloomberg Barclays U.S. Credit Index gained 0.52%, the Bloomberg Barclays U.S. Corporate High Yield Index advanced by 0.56% and the Bloomberg Barclays U.S. Treasury Index fell by -0.12%. TIPS showed gains for the month and muni bonds were among the best performers in the fixed income space in July.

Economic Data and Outlook

Economic readings continue to get more scrutinized as this expansion's length moves further into record territory. Information released in July, which largely covered the month of June, was rather mixed. The widely followed Institute for Supply Management (ISM) manufacturing index for June was modestly better than expected, but was a drop from the prior month. At an almost two-year low at 51.7, this reading has moved closer to the all-important 50 level over the last several months. Uncertainty in the global trade situation is likely impacting manufacturers, among other factors.

The ISM non-manufacturing index, which represents the much larger service industries in the U.S. economy, also dropped in June and was below expectations at 55.1. Recall that ISM readings above 50 indicate expansion and both readings remained in growth territory. Most housing data was below expectations as well.

However, retails sales (ex. auto and gas station sales) were stronger than expected in June, increasing by 0.7% for the month when a 0.3% gain was anticipated. Also, the first reading of second quarter GDP showed annualized growth of 2.1% when a 1.8% gain was expected. Job market data showed strong gains as well in June. Non-farm payroll additions were 224,000 in June, which was well ahead of the expectations of 160,000. The unemployment rate ticked a bit higher to 3.7% when it was expected to stay at 3.6%, but that coincided with an increase in the labor force participation rate as well. Average hourly earnings remained at 3.1% on a year-over-year basis in June when wages were expected to tick higher to 3.2%.

The dovish tone from the Fed, which has been a dominate theme this year, turned into action in July with the first rate cut since 2008. This cut has been widely expected since the June FOMC meeting. Rather than if the Fed would cut rate, the debate seemed to center around whether the Fed would lower rates by 25 or 50 basis points with little doubt a cut would occur at the July FOMC meeting.

Although we thought a cut was likely in July, we believed the expectations of 75-100 basis points of cuts over the next year were too aggressive under current conditions considering both first and second quarter GDP came in better than expected, the unemployment rate sits near a multi-decade low at 3.7% and stocks are near all-time highs. These market expectations could be a source of disappointment if the market and the Fed are out of step on the timing and amount of rate cuts. Some of the volatility we've seen early in August can be attributed to confusion following Chairman Powell's press conference when he seemed to dampen expectations of an extended period of rate cuts.

We continue to expect economic growth through 2019 and into 2020 and anticipate further market gains over the balance of the year. However, due to uncertainty in upcoming Fed policy decisions, unknowns on the trade front, and some slowing U.S. economic activity, we also believe that the range of outcomes for the market is wider than usual and volatility might come more to the forefront during the second half of 2019.

Event	Period	Estimate	Actual	Prior	Revised
ISM Manufacturing	June	51.0	51.7	52.1	—
ISM Non-Manf. Composite	June	56.0	55.1	56.9	—
Change in Nonfarm Payrolls	June	160k	224k	75k	72k
Unemployment Rate	June	3.6%	3.7%	3.6%	—
Average Hourly Earnings YoY	June	3.2%	3.1%	3.1%	—
JOLTS Job Openings	May	7470k	7323k	7449k	7372k
PPI Final Demand MoM	June	0.0%	0.1%	0.1%	—
PPI Final Demand YoY	June	1.6%	1.7%	1.8%	—
PPI Ex Food and Energy MoM	June	0.2%	0.3%	0.2%	—
PPI Ex Food and Energy YoY	June	2.1%	2.3%	2.3%	—
CPI MoM	June	0.0%	0.1%	0.1%	—
CPI YoY	June	1.6%	1.6%	1.8%	—
CPI Ex Food and Energy MoM	June	0.2%	0.3%	0.1%	—
CPI Ex Food and Energy YoY	June	2.0%	2.1%	2.0%	—

Event	Period	Estimate	Actual	Prior	Revised
Retail Sales Ex Auto and Gas	June	0.3%	0.7%	0.5%	—
Industrial Production MoM	June	0.1%	0.0%	0.4%	—
Building Permits	June	1300k	1220k	1294k	1299k
Housing Starts	June	1260k	1253k	1269k	1265k
New Home Sales	June	658k	646k	626k	604k
Existing Home Sales	June	5.32m	5.27m	5.34m	5.36m
Leading Index	June	0.1%	-0.3%	0.0%	—
Durable Goods Orders	June P	0.7%	2.0%	-1.3%	-2.3%
GDP Annualized QoQ	2Q A	1.8%	2.1%	3.1%	—
U. of Mich. Sentiment	July P	98.8	98.4	98.2	—
Personal Income	June	0.4%	0.4%	0.5%	0.4%
Personal Spending	June	0.3%	0.3%	0.4%	0.5%
S&P CoreLogic CS 20-City YoY NSA	May	2.40%	2.39%	2.54%	2.53%

Source: Bloomberg P=Preliminary A=Advanced

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The Dow Jones Industrial Average indicates the value of 30 large, publicly owned companies based in the United States.

The NASDAQ Composite is a stock market index of the common stocks and similar securities listed on the NASDAQ stock market.

The S&P 500 measures the performance of the 500 leading companies in leading industries of the U.S. economy, capturing 75% of U.S. equities.

The Russell 1000 Index measures the performance of the highest ranking 1,000 stocks in the Russell 3,000 Index, which represent about 90% of the total market capitalization of that index.

The Russell 2000 Index is a small-cap stock market index that represents the bottom 2,000 stocks in the Russell 3000.

The Russell 3000 Index measures the performance of the 3,000 largest U.S. companies based on total market capitalization, which represents approximately 98% of the investable U.S. equity market.

The MSCI Emerging Markets Index is used to measure large and mid-cap equity market performance in the global emerging markets.

The MSCI ACWI ex USA Index captures large and mid-cap representation across 22 of 23 developed market countries and 24 emerging market countries, covering approximately 85% of the global equity opportunity set outside of the U.S.

Bloomberg Barclays U.S. Aggregate Bond Index: The index is unmanaged and measures the performance of the investment grade, U.S. dollar denominated, fixed-rate taxable bond market, including Treasuries and government-related and corporate securities that have a remaining maturity of at least one year.

The Bloomberg Barclays U.S. Corporate High-Yield Index covers the U.S. dollar-denominated, non-investment grade, fixed-rate, taxable corporate bond market. Securities are classified as high-yield if the middle rating of Moody's, Fitch, and S&P is Ba1/BB+/BB+ or below.

The Bloomberg Barclays U.S. Credit Index measures the investment grade, U.S. dollar denominated, fixed-rate taxable corporate and government related bond markets.

ISM Manufacturing Index - A widely-watched indicator of recent U.S. economic activity. The index is often referred to as the Purchasing Manager's Index (PMI). Based on a survey of purchasing managers at more than 300 manufacturing firms by the Institute for Supply Management (ISM), the index monitors changes in production levels from month to month. The index is the core of the ISM Manufacturing Report.

The ISM Non-Manufacturing Index is an index based on surveys of more than 400 non-manufacturing firms' purchasing and supply executives, within 60 sectors across the nation, by the Institute of Supply Management (ISM). The ISM Non-Manufacturing Index tracks economic data, like the ISM Non-Manufacturing Business Activity Index. A composite diffusion index is created based on the data from these surveys, that monitors economic conditions of the nation.

The Composite Index of Leading Indicators, otherwise known as the Leading Economic Index (LEI), is an index published monthly by The Conference Board. It is used to predict the direction of global economic movements in future months. The index is composed of 10 economic components whose changes tend to precede changes in the overall economy. The Conference Board is an independent research association that provides its member organizations with economic and financial information.

The volatility (beta) of a client's portfolio may be greater or less than its respective benchmark. It is not possible to invest in these indices.

Index returns include the reinvestment of income and dividends. The returns for these unmanaged indexes do not include any transaction costs, management fees or other costs. It is not possible to make an investment directly in any index.

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