Brinker Capital

WEEKLY WIRE | JULY 8, 2019

# Fortunately, there's no rule about not talking about "The Rule of 20"

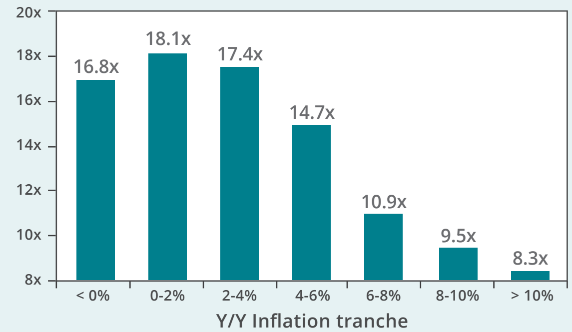

Coming into 2019, Brinker Capital believed if we could solve for monetary policy risk and trade policy risk that the economy and the markets would be biased higher. Well, we received more good news than bad on both fronts lately, and risk assets and the economy have responded, with the S&P 500 Index (S&P 500) up about 19% YTD and the US economy growing a better than expected 3.2% in Q1 (though the pace of economic growth likely slowed in the second quarter). Having written that, the very strong first half stock market rally has many investors wondering whether US equities can move higher from here.

One way to think about market valuation and potential price appreciation is via "The Rule Of 20." Simply put, The Rule Of 20 states a reasonable multiple for the market can be determined by deducting the rate of inflation from the number 20. The reason The Rule carries weight on Wall Street is historically the market's P/E Ratio (i.e. multiple) has more or less followed the formula (see the chart on the right); the caveat being The Rule doesn't prove relevant during periods of deflation. Once we have the P/E ratio, we simply multiply by expected earnings to arrive at a price target for the index (and in turn, the broader market).

Well, inflation - as measured by the Consumer Price Index - is running just below 2%, and Wall Street expects earnings for the S&P 500 on a forward four quarter basis to total approximately $175. So, an 18 P/E ratio on $175 produces a price target of 3,150 for the S&P 500 and additional gains, from today's price, of about 6.0%.

If we solve for monetary policy risk and trade policy risk, and we think we will, US equities should continue to move higher into year end.

S&P 500 average trailing P/Es by inflation tranche




Equities, oil & natural gas (7/5/19)

| Security name | Last | QTD chg | YTD chg | 12mo chg |
|---|---|---|---|---|
| S&P 500 | 2990.41 | 1.65% | 19.29% | 8.36% |
| Russell 2000 | 1575.62 | 0.58% | 16.84% | -6.99% |
| Russell 3000 Growth | 1307.29 | 1.97% | 23.02% | 9.17% |
| Russell 3000 Value | 1668.97 | 1.21% | 15.95% | 4.45% |
| Crude Oil WTI (NYM $/bbl) | 57.73 | -1.27% | 27.13% | -21.78% |
| Natural Gas | 2.40 | 3.90% | -15.89% | -16.10% |

Treasury rates (7/5/19)

| | Price | Yield |
|---|---|---|
| 2Y | 99.172 / 99.17 | 1.859 |
| 3Y | 99.266 / 99.27 | 1.802 |
| 5Y | 99.192 / 99.19 | 1.832 |
| 7Y | 99.224 / 99.23 | 1.920 |
| 10Y | 103.002 / 103.0 | 2.036 |
| 30Y | 106.310 / 107.0 | 2.540 |

Weekly reports

**This week**
- NFIB Small Business Index
- Initial Claims

**Last week**
- Hourly Earnings Y/Y 3.1%
- Unemployment Rate 3.7%

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# Brinker Capital Market Barometer

JULY 2019

The weight of the evidence shifted even further into positive territory. Our modest overweight to risk drifted higher in June, aligning portfolios with this view.

## SHORT-TERM FACTORS (< 6 months)

| | CHANGE | NEGATIVE | NEUTRAL | POSITIVE | |
|---|---|---|---|---|---|
| Momentum | → | | | ● | Market momentum strengthened |
| Trend | → | | ● | | Global equity indices moved above ST and LT moving averages |
| Investor sentiment | | | ● | | Investor sentiment surveys more optimistic but fund flows muted |
| Seasonality | ←← | ● | | | Third quarter historically weakest for equities |

## INTERMEDIATE-TERM FACTORS (6-36 months)

| | CHANGE | NEGATIVE | NEUTRAL | POSITIVE | |
|---|---|---|---|---|---|
| Fiscal policy | | | | ● | Fiscal stimulus expected to increase leading up to 2020 election |
| Monetary policy | | | | ● | Expectations for a Fed rate cut; global central banks more accommodative |
| Inflation | → | | | ● | Global inflation low and slowing; inflation expectations muted |
| Interest rate environment | | | ● | | Longer-term rates range-bound; yield curve inversion at short end |
| Macroeconomic | | | ● | | US growth solid but ex-US growth weaker; global trade war concerns |
| Business sentiment | | | ● | | Small business confidence off record high; CEO confidence little improved |
| Consumer sentiment | | | | ● | Remains at elevated levels; still supportive |
| Corporate earnings | | | | ● | US earnings growth still solid; softer outside US |
| Credit environment | | | | ● | Credit spreads have tightened |

## LONG-TERM FACTORS (36+ months)

| | CHANGE | NEGATIVE | NEUTRAL | POSITIVE | |
|---|---|---|---|---|---|
| Valuation | | | ● | | US equity valuations at long-term averages; more attractive ex-US |
| Business cycle | | | | ● | Long recovery but has been muted; few signs point to recession |
| Demographics | | | ● | | Mixed (US and emerging markets positive; developed intl negative) |

Source: Brinker Capital. Information is accurate as of July 2, 2019. Themes and specific funds utilized to implement themes are discussed within the context of Brinker Capital's managed asset allocations and are based on current market conditions and constitute Brinker Capital's judgment and opinions, which are subject to change without notice. Past performance does not guarantee future results. Statements referring to future actions or events, such as the future financial performance of certain asset classes or market segments, are based on the current expectations and projections about future events provided by various sources, including Brinker Capital's Investment Management Group. These statements are not guarantees of future performance and actual events may differ materially from those discussed. Brinker Capital Inc., a registered investment advisor.